

VOLUME 4, CHAPTER 27: "INTERNAL USE SOFTWARE"*SUMMARY OF MAJOR CHANGES**

All changes are denoted by **blue font**.

Substantive revisions are denoted by an asterisk (*) symbol preceding the section, paragraph, table, or figure that includes the revision.

Unless otherwise noted, chapters referenced are contained in this volume.

Hyperlinks are denoted by **bold, italic, blue, and underlined font**.

This is the initial publication.

PARAGRAPH	EXPLANATION OF CHANGE/REVISION	PURPOSE
Various	This chapter contains updated policy for internal use software (IUS) based upon IUS policy contained in Volume 4, Chapter 6, dated June 2009. As a result, the existing policy in Volume 4, Chapter 6 related to IUS is no longer applicable.	Revision
Various	The Federal Accounting Standards Advisory Board issued a new accounting standard for leases with an effective date for reporting periods beginning after September 30, 2020. Policy has yet to be fully developed to implement this new standard, which may result in changes to the capital lease criteria. Until the new standard becomes effective, the policy guidance in this chapter must be followed.	Revision
Policy Memo	The Deputy Chief Financial Officer policy memorandum, "Strategy for Internal Use Software Audit Readiness," dated September 30, 2015 has been incorporated into the chapter as applicable and is cancelled.	Cancellation
270103	Added "Authoritative Guidance" paragraph.	Addition
270201	Added a definition for software and additional guidance for distinguishing internal use software from integrated software.	Addition
270202	Added relevant United States Standard General Ledger accounts and their descriptions.	Addition

PARAGRAPH	EXPLANATION OF CHANGE/REVISION	PURPOSE
270203	Updated guidance for capitalized costs of internally developed software; treatment of software development costs; software developed by one activity and used by others without reimbursement; software development phases; and documentation. Added guidance for different software development methods; cross-functional Internal Use Software (IUS) reviews; determining accounting treatment of different software development activities; and capitalizable cost.	Revision/ Addition
270204	Updated guidance for recognition responsibility, including recognition timing of contractor acquired property and progress payments. Updated capitalization threshold amounts and capitalization guidance. Revised recognition guidance for bulk purchases of software. Added guidance for IUS developed through a joint venture; for software licenses; cloud and other subscription based services, shared services; and guidance on accountable records of IUS.	Revision/ Addition
270205	Added guidance addressing IUS enhancements.	Addition
270206	Updated guidance for maintenance and repair of IUS.	Revision
270207	Added guidance addressing amortization of IUS.	Addition
270208	Added guidance addressing impairment of IUS.	Addition
270209	Updated guidance addressing the removal/disposal of IUS.	Revision
270301	Added guidance on the use of the "Canceled" Treasury Account Symbol.	Addition
270303	Added guidance for reporting requirements.	Addition
Figure 27-2	Added a capitalization decision tree for IUS.	Addition
Annex 1	Added an annex containing common terms used by information technology and software programming professionals, with corresponding examples, that are relevant to IUS.	Addition
Annex 2	Added guidance for use as an alternative methodology for establishing opening balances for IUS.	Addition

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CHAPTER 27*INTERNAL USE SOFTWARE**

2701 GENERAL

270101. Overview

A. This chapter prescribes Department of Defense (DoD) accounting policy for **Internal Use Software (IUS)**, which is a subset of General Property, Plant, and Equipment (PP&E). **This overview paragraph will define and describe the characteristics of General PP&E.**

B. General PP&E **items** are used in providing goods or services, or support the mission of the entity, and **typically have** one or more of **the following** characteristics:

1. **The item** could be used for alternative purposes (e.g., by other DoD or Federal Programs, state or local governments, or nongovernmental entities), but it is used to produce goods or services, or to support the mission of the entity;

2. **The item** is used in business-type activities; **and/or**

3. **The item** is used by entities in activities whose costs can be compared to those of other entities performing similar activities (e.g., federal hospital services in comparison to commercial hospitals).

270102. Purpose

The applicable general ledger accounts are listed in the government-wide United States Standard General Ledger (USSGL) contained in Volume 1, Chapter 7. The accounting entries for these accounts **and the DoD Standard Chart of Accounts** are specified in the **DoD USSGL Standard Transaction Library**. Unless otherwise stated, this chapter is applicable to all DoD Components, including **Working Capital Fund (WCF)** activities.

*270103. Authoritative Guidance

The accounting policy and related requirements prescribed by this chapter are in accordance with the applicable provisions of:

A. Federal Accounting Standards Advisory Board (FASAB) Statement of Federal Financial Accounting Concepts (**SFFAC 5**), “Definitions of Elements and Basic Recognition Criteria for Accrual-Basis Financial Statements;”

B. FASAB **SFFAC 7**, “Measurement of the Elements of Accrual-Basis Financial Statements in Periods After Initial Recording;”

C. FASAB Statement of Federal Financial Accounting Standards (**SFFAS 1**), “Accounting for Selected Assets and Liabilities;”

- D. FASAB SFFAS 4, “Managerial Cost Accounting Standards and Concepts;”
- E. FASAB SFFAS 10, “Accounting for Internal Use Software;”
- F. FASAB SFFAS 50, “Establishing Opening Balances for General Property, Plant, and Equipment: Amending Statement of Federal Financial Accounting Standards (SFFAS) 6, SFFAS 10, and SFFAS 23, and Rescinding SFFAS 35;”
- G. FASAB Technical Release (TR 13), “Implementation Guide for Estimating the Historical Cost of General Property, Plant, and Equipment;”
- H. FASAB TR 14, “Implementation Guidance on the Accounting for the Disposal of General Property, Plant & Equipment;”
- I. FASAB TR 15, “Implementation Guidance for General Property, Plant, and Equipment Cost Accumulation, Assignment and Allocation;”
- J. FASAB TR 16, “Implementation Guidance for Internal Use Software;”
- K. FASAB TR 17, “Conforming Amendments to Technical Releases for SFFAS 50, Establishing Opening Balances for General Property, Plant, and Equipment;”
- L. FASAB TR 18, “Implementation Guidance for Establishing Opening Balances;”
- M. Office of Management and Budget Circular No. A-136, “Financial Reporting Requirements;”
- N. DoD Instruction (DoDI 5000.76); “Accountability and Management of Internal Use Software (IUS);” and
- O. Treasury Financial Manual (TFM) Volume1, Part 2, Chapter 4700 "Agency Reporting Requirements for the Financial Report of the United States Government."

2702 ACCOUNTING FOR IUS

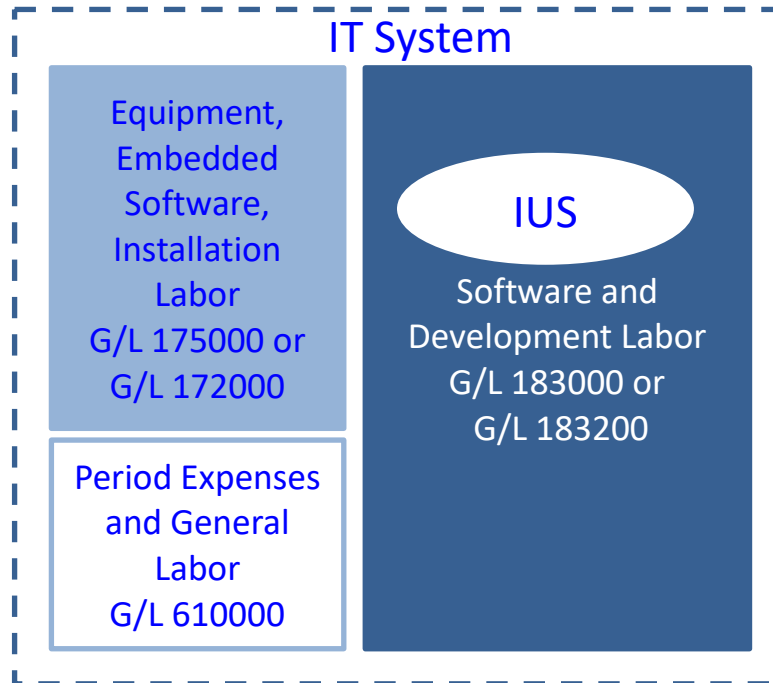
*270201. Definition

A. “Software” includes the application and operating system programs, procedures, rules, and any associated documentation pertaining to the operation of a computer system or program. Most often, software is an integral part of an overall system(s) having interrelationships between software, hardware, personnel, procedures, controls, and data. IUS is software that:

- 1. Is acquired or developed to meet the entity’s internal or operational needs (*intended purpose*); and

2. Is a stand-alone application, or the combined software components of an information technology (IT) system that can consist of multiple applications, modules, or other software components integrated and used to fulfill the entity's internal or operational needs (*software type*).

Figure 27-1. IUS is Generally One Component of an IT System



B. IUS can be:

1. Purchased from commercial off-the-shelf (COTS) vendors and be ready for use with little or no changes;
2. Internally developed by employees of DoD, including new software and existing or purchased software that is modified with or without a contractor's assistance; or
3. Contractor-developed software that a DoD Component paid a contractor to design, program, install, and implement, including new software and the modification of existing or purchased software.

C. IUS includes software that is:

1. Used to operate an entity's programs (e.g., financial and administrative software, including that used for project management);

2. Used to produce the entity's goods and to provide services (e.g., maintenance work order management and loan servicing); and

3. Developed or obtained for internal use and subsequently provided to other Federal Entities with or without reimbursement.

D. Integrated (embedded) software is not IUS.

1. IUS does not include computer software that is integrated into and necessary to operate General PP&E, rather than perform an application. Such software must be considered part of the PP&E of which it is an integral part, and capitalized and amortized accordingly (e.g., [software embedded in airport radar, computer-operated lathes, military equipment/weapon systems and special test equipment](#)). The aggregate cost of the hardware and software must be used to determine whether to capitalize or expense the costs. In situations where software and the hardware on which it runs have independent service lives, the determination of the useful life of the software must be viewed independently of the useful life of the hardware. The determination must be made on a case-by-case basis. The rationale for this determination must be documented.

2. Software used in conjunction with the operation of equipment, which is not the same as the integrated or embedded software, can be considered IUS if all of the following criteria apply:

- a. [The software was developed separately from the equipment;](#)
- b. [The software is not required for the equipment to perform its core purpose and functions; and](#)
- c. [The quantity of equipment items on which the software will be installed is unknown.](#)

E. DoD entities [may purchase IUS](#) as part of a package of products and services (e.g., training, maintenance, data conversions, reengineering, site licenses and rights to future upgrades and enhancements). [If the costs are not readily separable between the IUS and the services on the invoice, contract or other procurement documents, costs should be allocated based on the relative fair values of the IUS and the services. The cost of the IUS should be capitalized \(assuming it meets the capitalization criteria\) and the cost of the training/maintenance should be expensed.](#) Non-IUS costs (e.g., training and maintenance services) that are not susceptible to allocation between maintenance and relatively minor enhancements must be expensed.

F. Materiality, as defined by the SFFAS 1, is the degree to which an item's omission or misstatement in a financial statement makes it probable that the judgment of a reasonable person relying on the information would have been changed or influenced by the inclusion or correction of the item.

G. Additional definitions can be found in Annex 1.

*270202. Relevant USSGL Accounts

A. Fund Balance with Treasury (Account 101000). This account is used to record the aggregate amount of funds on deposit with the United States Department of the Treasury, excluding seized cash deposited.

B. Internal Use Software (Account 183000). This account is used to record the amount of capitalized cost of IUS for those costs that are to be capitalized in accordance with Table 27-1. It includes (1) purchased COTS software, (2) contractor-developed software, and (3) internally developed software.

C. Internal Use Software in Development (Account 183200). This account is used to record the full cost amount incurred for those costs that are to be capitalized in accordance with Table 27-1 during the software development phase of (1) contractor-developed software and (2) internally developed software, (as defined in SFFAS 10). Upon completion, these costs will be transferred to USSGL account 183000, Internal Use Software. There is no Generally Accepted Accounting Principles (GAAP) requirement to establish a separate account for each software under development. However, DoD Components may elect to create separate subaccounts to better differentiate and track costs.

D. Accumulated Amortization on Internal Use Software (Account 183900). This account is used to record the accumulated amount of amortization charges to expense for IUS.

E. General Property, Plant, and Equipment Permanently Removed but Not Yet Disposed (Account 199500). The General Property, Plant, and Equipment Permanently Removed but Not Yet Disposed account is used to record the value of General PP&E assets that have been permanently removed from service. Upon permanent removal from service, IUS assets must be recorded at their expected net realizable value (NRV) and must cease to be amortized. See paragraph 270209 for guidance on reporting IUS assets that have been permanently removed from service.

F. Gains on Disposition of Assets – Other (Account 711000). This account is used to record the gain on the disposition (such as sale, exchange, disposal, or retirement) of assets not associated with investments or borrowings/loans.

G. Losses on Disposition of Assets – Other (Account 721000). This account is used to record the loss on the disposition (such as sale, exchange, disposal, or retirement) of assets not associated with investments or borrowings/loans.

*270203. Acquisition/Valuation

A. Recorded Cost. When acquiring IUS, the acquisition cost and other costs necessary to bring the software to an operable condition must be recognized in accordance with paragraph 270204.

1. COTS Software. The capitalized cost of COTS software **must** be the actual purchase price, plus any costs incurred to place the software in service or otherwise make the software ready for use.

2. Contractor-Developed Software. The capitalized cost of contractor-developed software **must** include the amount paid to the contractor to design, program, install, and implement new software or to modify existing or COTS software, plus any costs incurred to implement or otherwise make the software ready for use.

3. Internally Developed Software. The capitalized costs of internally developed software **must** include the full cost (direct and indirect costs, as described in subparagraphs 270203.A.4.a, 270203.A.4.b and 270203.A.4.c) incurred after:

a. The DoD Component authorizes and commits to a software project and believes that it is more likely than not that the project will be completed and the software will be used to perform the intended function(s), and it will have an estimated service life of two years or more; and

b. The completion of the conceptual planning/planning and requirements phase (i.e., project evaluation, concept testing, and evaluation alternatives) as evidenced by a documented approval decision.

4. Table 27-1. This table provides a matrix of the software project phases and their related processes. The treatment of costs **must** be applied based on the nature of the costs incurred, not the exact sequence of the work. Full cost includes the costs of new software (e.g., salaries of programmers, systems analysts, project managers, and administrative personnel; associated employee benefits; outside consultants' fees; rent; and supplies and overhead) and technical documentation. The development of technical documentation and manuals **must** be capitalized, **but** the costs of mass-producing manuals **should be** expensed in the period incurred. The various types of costs incurred during the software project phases include:

a. Direct Labor Costs. Direct labor costs are typically the labor costs of project teams (e.g., programmers, engineers, managers) incurred during the Design/Development and Testing/Implementation Phase and are capitalized as part of the costs of the software project. Project managers and/or program managers **must** track direct labor cost and allocate to individual software projects. The allocation methodology **must** be consistent between projects and **must** be auditable.

b. Indirect Labor Costs. Indirect labor costs are typically the labor costs associated with the Program Management Office (PMO) personnel responsible for overseeing more than one software project. In many instances, PMO indirect labor costs are immaterial when compared with the overall costs of a software project, and if determined to be immaterial, **can** be expensed. Decisions regarding the materiality of indirect labor costs, when such costs are expensed, **must** be justified, documented, and **must be able to** stand up to audit scrutiny. If indirect labor costs are determined to be material to a software project or projects and are to be distributed to the capitalized costs of such project, the costs **must** be allocated based on a distribution methodology that is consistently applied, documented and auditable.

c. Overhead Costs. Overhead costs are those costs associated with utilities, building maintenance, and supplies that are essential to the overall accomplishment of a software project. In many instances, overhead costs are immaterial when compared with the overall costs of a software project and if determined to be immaterial, [the DoD Components should expense these costs](#). Decisions regarding the materiality of overhead costs when such costs are to be expensed must be justified, documented, and must [be able to](#) stand up to audit scrutiny. If overhead costs are determined to be material to a software project or projects and are to be distributed to the capitalized costs of such project, the costs [must](#) be allocated based on a distribution methodology that is [consistently applied](#), documented and auditable.

d. Contractor Costs. Contractor costs must be evaluated to determine whether the costs are to be expensed or capitalized. Such determination is based on the type of work performed by the contractors. [Table 27-1](#) provides a breakdown of the various work activities and whether the cost of such activities must be expensed or capitalized.

e. Data Conversion Costs. All data conversion costs incurred for internally developed, contractor developed, or COTS software must be expensed as incurred, including the cost to develop or obtain software that allows for access or conversion of existing data to the new software. Such costs may include the purging or cleansing of existing data, reconciliation or balancing of data, and the creation of new or additional data.

B. Software Development Phases Determine Recorded Cost (Internally Developed Software). Software's life-cycle phases include planning, development, and operations. This subparagraph provides a framework for identifying software development phases and processes to help isolate the capitalization period for IUS that the DoD entity is developing. The three phases of software development described in subparagraph follow a linear software development method. Generally, costs incurred during the development phase are to be capitalized and costs incurred in other phases are to be expensed. However, software development under other methods does not follow this linear approach and capitalization decisions absent distinct phases are more difficult. Regardless of timing, the cost incurred for development phase activities must be capitalized or expensed based on their substance/task activity rather than their phase. The three phases of software development are:

1. Conceptual Planning/Planning and Requirements Phase. In this phase, the DoD Components will most likely do the following:

a. Make strategic decisions to allocate resources between alternative projects at a given time. For example, should programmers develop new software or direct their efforts toward correcting problems in existing software?

b. Determine performance requirements (i.e., what it is that they need to do)?

c. Invite vendors to perform demonstrations of how their software will fulfill a DoD Component's needs.

d. Explore alternative means of achieving specified performance requirements. For example, should a DoD Component make or buy the software? Should the software run on a mainframe or client server system?

e. Determine that the technology needed to achieve performance requirements exists.

f. Select a vendor if a DoD Component chooses to obtain COTS software.

g. Select a consultant to assist in the software's development or installation.

2. Software Design/Development and Testing/Implementation Phase. In this phase, the DoD Components will likely to do the following:

a. Use a system to manage the project;

b. Track and accumulate life-cycle cost and compare it with performance indicators;

c. Determine the reasons for any deviations from the performance plan and take corrective actions;

d. Test the deliverable to verify that they meet the specifications.

3. Operations and Maintenance/Disposition Phase. In this phase, the DoD Components will likely to do the following:

a. Operate the software, undertake preventative maintenance, and provide ongoing training for users;

b. Convert data from the old to the new system;

c. Undertake post-implementation review comparing asset usage with the original plan; and/or

d. Track and accumulate life-cycle cost and compare it with the original plan.

Table 27-1. Capital versus Expense IUS Activities
(Adapted from SFFAS 10, paragraph 11)

Project Phase	Task	Treatment
Conceptual Planning/ Planning & Requirements	Project Evaluation	Expense
	Concept testing	Expense
	Evaluation of alternatives	Expense
	Project approval	Expense
Design/ Development & Testing/ Implementation	Design	Capitalize
	Coding	Capitalize
	Installation to Hardware	Capitalize
	Project personnel costs	Capitalize
	Technical Acceptance Testing	Capitalize
	Quality assurance testing	Capitalize
	Documentation	Capitalize
	Overhead costs	Allocate
	Data conversion software	Expense
Operations & Maintenance/ Disposition	Training	Expense
	Data conversion	Expense
	Help desk	Expense
	Enhancement	See "IUS Enhancements" paragraph 270205.
	Maintenance/Bug Fix	Expense
PROGRAM MANAGEMENT		
The costs of program management and the PMO that may be incurred during each phase of software development or acquisition are indirect costs. PMO indirect costs should be expensed or capitalized, depending on: 1) their materiality to overall costs of individual software development projects, and 2) in which phase the costs are incurred.		

C. Software Development Methods. Software development methods are ever evolving, with new methods and techniques being introduced over time. Included in the following subparagraphs are several descriptive examples of common software development methods.

1. Linear/Waterfall Software Development Method. The linear/waterfall software development method is a sequential design process, used in software development in which progress is seen as flowing steadily downwards (like a waterfall) through the software development phases. The linear/waterfall software development method follows the phases outlined in Table 27-1 in sequence, whereas the other software development methods as described in subparagraphs 270203.C.2 through 270203.C.4 can move between phases during the life of the development. Regardless of the development method (e.g., waterfall, prototyping, agile, or spiral), the capitalization decisions follow the tasks identified.

2. Prototyping Software Development Method. The prototyping software development method is a system development method in which a prototype (an early approximation of a final system or product) is built, tested, and then reworked as necessary until an acceptable prototype is finally achieved from which the complete system or product can be developed. This model works best in scenarios where not all of the project requirements are known in detail ahead of time. An iterative, trial-and-error process takes place between the developers and the users.

3. Agile Software Development Method. The agile software development method is a group of software development methods in which requirements and solutions evolve through collaboration between self-organizing, cross-functional teams.

a. In an agile project, working software is deployed in iterations of typically one to eight weeks in duration, each of which provides a segment of functionality. Initial planning regarding cost, scope, and timing is usually conducted at a high level, and the project status is primarily evaluated based on software demonstrations.

b. The IUS development phases listed in subparagraph 270203.B could be applied to agile development projects on an iteration basis. If an iteration developed meets the module or component asset description in accordance with subparagraph 270203.F.3 and the capitalization cut-off period described in subparagraph 270203.F.6, then it could be treated as an individual IUS project. If the numbers of iterations are dependent on the outcomes of multiple processes for a complete function, the cost incurred in these iterations should be grouped together based on the nature of the activities (capital or expense) and treated as one project for the purposes of recognition, measurement, and disclosure. Any future incremental releases that result in additional functionality can be treated as an enhancement of the original IUS project and accounted for in accordance with paragraph 270205.

4. Spiral Software Development Method. The spiral software development method combines the features of the waterfall and prototyping incremental models, but with more emphasis placed on risk analysis and management.

a. The spiral methodology projects are typically separated into phases like the waterfall method: planning, risk analysis, engineering, and evaluation. However, they are broken up into incremental releases of the product, or incremental refinement through each time around the spiral and through continuously analyzing the requirements and improving the definition and implementation. At each iteration around the cycle, the project is improved and extended.

b. The IUS development phases listed in subparagraph 270203.B could be applied to a spiral development project on a process iteration basis. If an iteration developed meets the module or component asset description in accordance with subparagraph 270203.F.3 and the capitalization cut-off period described in subparagraph 270203.F.6, then it could be treated as an individual IUS project. If the number of iterations are dependent on the outcomes of multiple spiral processes for a complete function, the cost incurred in these iterations should be grouped together based on the nature of the activities

(capital or expense) and treated as one project for the purposes of recognition, measurement, and disclosure. Any future incremental releases that result in additional functionality can be treated as an enhancement of the original IUS project and accounted for in accordance with paragraph 270205.

D. Cross-Functional IUS Reviews. Software development can be complex and accounting decisions often require a measure of judgment and expertise found throughout an organization. Examples of these decisions can include identifying assets that meet the IUS definition, determining the point at which an IUS project is more likely than not to be completed, whether an enhancement should be capitalized, and determining the useful life. DoD Components will ensure that key stakeholders from the IUS program, acquisition, and accounting organizations have adequate visibility into the major milestones throughout the acquisition process to make these decisions. This could take the form of an IUS acquisition review board, consisting of knowledgeable stakeholders who assess pending and active IUS projects to make such decisions. It could also include leveraging portfolio management processes already in place at some DoD Components. Stakeholders will meet periodically and with enough frequency to make timely decisions concerning the IUS and the decisions will be documented. Additional cross-functional decisions and deadlines for making them are found in Table 27-2. This review activity can also serve as a key control.

Table 27-2. Cross-Functional Review Decisions and Timeline

Decision	Decision Timeline
Identify potential IUS	During the budget process and not later than end of planning phase
Determine that it is more likely than not that the IUS project will be completed	Prior to the completion of the planning phase
Assign a useful life	Prior to the end of final technical acceptance testing
Confirm that cost has been correctly accumulated and assigned to the asset	Prior to the end of final technical acceptance testing
Confirm that indirect costs have been appropriately allocated	Prior to the end of final technical acceptance testing
Assign an in-service date	Upon completion of final technical acceptance testing
Determine if licenses meet capital lease criteria	Upon license agreement execution
Decision	Decision Timeline
Identify potential capital enhancements	During the budget process and not later than end of planning phase
Management Oversight Decisions <ul style="list-style-type: none"> • Impairment • Evaluation of suspended projects <ul style="list-style-type: none"> o More likely than not that the project will be completed o More likely than not that the project will be cancelled 	On-going

E. Capital Versus Expense IUS Activities. Many IUS programs and contracts include a variety of activities that are conducted by government and/or contractor personnel throughout the software development life cycle. Some costs associated with these activities should be capitalized as part of the cost of the IUS and some costs should be expensed. Regardless of the software development method (e.g., waterfall, prototyping, agile, or spiral), the capitalization decisions follow the activity. When reviewing contracts and budget documentation, care must be taken to distinguish between activities that are to be capitalized and those that are to be expensed. Refer to Table 27-1 for additional details on capital versus expense for IUS activities.

F. Capitalizable Cost

1. DoD Components must capitalize the cost of software when such software meets the criteria for General PP&E (see subparagraph 270204.E).

2. Costs related to capitalized activities identified in Table 27-1 must be accumulated in account 183200 (Internal Use Software in Development), but are not amortized until the software is placed-in-service. Costs should begin accumulating in this account if the IUS is anticipated to meet capital criteria and the criteria listed in subparagraph 270203.A.3 have been met.

3. Accumulated costs must be transferred to account 183000 (Internal Use Software) when the IUS is placed-in-service (see placed-in-service dates in subparagraph 270207.C). Many larger and more complex software systems, such as Enterprise Resource Planning systems, are developed and placed-in-service over time. For each module or component of a software project, costs must be moved from account 183200 (Internal Use Software in Development) to account 183000 (Internal Use Software), and amortization must begin when a module or component has been successfully tested. If the use of a module is dependent on the completion of another module(s), the movement from 183200 to 183000 will take place and amortization will begin when both that module and the other module(s) have successfully completed testing. For example, a DoD Component may develop an accounting software system containing three modules: a general ledger, an accounts payable sub-ledger, and an accounts receivable sub-ledger. In this example, each module could be analyzed to determine whether it could be treated as a separate IUS asset. Specifically, if the module provides economic benefit through distinct, substantive functionality, and meets the tests for capitalization threshold, ownership, and eligibility for capital treatment, then the module could be treated as a separate IUS asset.

4. Capitalized IUS costs must have sufficient supporting documentation as discussed in paragraph 270302, including support for costs incurred in the development of the IUS. Documentation in the form of narratives, software architectural documentation, user manuals and other similar documents supporting the functionality of the components/modules of a software system must be available to substantiate whether the IUS should be treated as separate IUS assets.

5. The full cost (direct and indirect cost as described in subparagraphs 270203.A.4.a through 270203.A.4.d) incurred during the software development phase must be

capitalized. Considering economic feasibility, a cost estimation technique could be developed to trace the costs to outputs based on the SFFAS 4, paragraph 124, provision that “[in] principle, costs should be assigned to outputs in one of the methods listed in the order of preference:

- a. Directly tracing costs wherever economically feasible;
- b. Assigning costs on a cause-and-effect basis; and
- c. Allocating costs on a reasonable and consistent basis.

6. Costs incurred after final **technical** acceptance testing has been successfully completed **must** be expensed (see Table 27-1). **Technical** acceptance testing is testing undertaken to verify if a software product meets **technical** specifications. **Technical acceptance testing costs are capitalizable costs**. Operational testing and evaluation and other functional testing conducted after technical acceptance **must** be expensed. **Similarly, if the software consists of multiple individual components or modules, the capitalization phase must end for each component/module after technical acceptance testing is complete for that component/module**. In some development practices, each iteration within an IUS development has its own acceptance testing before moving forward to the next iteration and final acceptance testing may not always be performed. The entity should identify a pre-determined agency milestone such as the go-live or in-service date, which is equivalent to a final technical acceptance test for capitalization cut-off purposes.

7. For COTS software, capitalized costs must include the amount paid to the vendor for the software. For contractor-developed software, capitalized costs must include the amount paid to a contractor to design, program, install, and implement the software. Material internal costs incurred by the Federal Entity to implement the COTS or contractor-developed software and otherwise to make it ready for use must be capitalized.

G. Documentation

1. When recording the acquisition of IUS in the **Accountability Property System of Record (APSR)** and/or accounting system, the **software** must be assigned a dollar value (i.e., recorded cost) as detailed in this chapter. **Appropriate documentation must be available to support the dollar value**. Paragraph 270302 includes a complete discussion of supporting documentation related to IUS.

2. To establish proper PP&E financial control when acquiring IUS from another DoD Component or Federal Agency, the acquiring DoD Component must request from the losing DoD Component or other Federal Agency, the necessary source information and financial transfer documents, to include unique identifier(s) for the **software(s)**; location; original acquisition cost(s); cost of **enhancements**; the date the **software was developed**, or acquired; the estimated useful life; the amount of accumulated **amortization**; and other relevant information linked to that **software**. If this information is not available, the gaining and losing entities must develop and document a **reasonable** estimate to support the financial transfer of the **software**.

*270204. Recognition

DoD Components must recognize all acquired IUS for accountability and financial reporting purposes. Recognition requires the proper accounting treatment (expense or capitalization with amortization) and the reporting of capitalized amounts and accumulated amortization on the appropriate DoD Component's financial statements. For financial reporting purposes, all IUS that has a useful life of two years or more and meets the capitalization criteria described in subparagraph 270204.E must be capitalized. IUS that does not meet the capitalization threshold must be expensed.

A. Recognition Responsibility

1. The DoD Component's financial reporting responsibility can be determined using a two tier criteria:

a. Exclusive/sole Use. When a DoD Component is the exclusive/sole user of capitalized IUS, it will report the IUS on its Balance Sheet. If there is no exclusive/sole user, the DoD Component must apply the second criteria.

b. Control. If an exclusive/sole user does not exist, the DoD Component that controls the IUS will have financial reporting responsibility. Evidence of control can include funding the software maintenance, exercising access control, and prioritizing enhancements.

2. DoD Components that possess and/or control IUS items that materially contribute to the Component's mission must maintain accounting and financial reporting for such items, regardless of the organization that originally acquired or provided the funding for the items. If a DoD Component prepares financial statements, such IUS items must be appropriately recognized in its financial statements.

B. Recognition Uncertainty

1. It is important that the overall accounting records of the DoD and the Federal Government are not duplicative. In situations where doubt exists as to which DoD Component should recognize an item, DoD Components involved must reach agreement with the other applicable DoD Components or Federal agencies as to which entity will recognize the item. The process used to reach this agreement and the terms of the agreement must be documented in a memorandum of agreement and be considered supporting documentation.

2. If an agreement cannot be reached, the matter must be referred to the Office of the Deputy Chief Financial Officer, Office of the Under Secretary of Defense (Comptroller) for resolution. Requests for resolution must be accompanied by adequate supporting documentation to assist in resolution of the matter and be submitted through the Financial Management and Comptroller of the submitting Military Department or Defense Agency.

C. Recognition Timing

1. Recognition of the COTS IUS for financial reporting purposes must occur no later than the technical acceptance of the software.

2. IUS in development must be recorded in the Internal Use Software in Development account (USSGL 183200) during the design, development and testing, and implementation phases. After technical acceptance testing is completed, an IUS asset will be recognized, capital costs will be transferred to the Internal Use Software account (USSGL 183000), and accountability must be established in the APSR.

3. For IUS assets acquired by a contractor on behalf of a DoD Component (i.e., the DoD Component that will ultimately hold title/license to the assets), the software must be recognized upon completion of the technical acceptance testing by the contractor performing the service, or by the DoD Component. Contract financing payments (e.g., progress payments, performance-based payments, and commercial interim payments) made to a contractor prior to completion of final technical acceptance testing must be recorded in a Software in Development account until the IUS is placed-in-service. Upon completion of technical acceptance testing, the Contractor Acquired Property (CAP) must be capitalized in the appropriate USSGL account. See subparagraph 270203.F for guidance on the use of the Software in Development account.

D. Capitalization Thresholds

1. The current IUS capitalization threshold for all DoD Components is \$250,000, except for the Office of the Director of National Intelligence, for which the capitalization threshold is \$1 million.

2. IUS with a cost that equals or exceeds the appropriate capitalization threshold must be capitalized according to subparagraph 270204.E as an asset in the appropriate DoD Component's accounting records and amortized over its useful life. IUS items with a cost below the appropriate capitalization threshold must be expensed; with the exception of IUS items acquired as part of a qualifying bulk purchase (see subparagraph 270204.G).

3. The capitalization threshold described in subparagraph 270204.D.1 is for financial reporting purposes. The requirement for accountability of IUS is discussed in subparagraph 270204.K.

E. Capitalization Criteria

1. IUS is recognized and capitalized if it meets the following criteria for General PP&E:

a. Useful life of two years or more;

b. Intended for use or being available for use by the entity;

- c. Not intended for sale in the normal course of business; and
- d. Total cost is greater than DoD Component's capitalization threshold (as described in subparagraph 270204.D).

2. As development work accumulates, the costs must be entered into an Internal Use Software In Development account (183200). When the IUS passes final technical acceptance testing, the accumulated costs must be removed from the "In Development" account and transferred to the Internal Use Software account (183000). Accounting entries for this account are specified in the DoD USSGL Transaction Library.

F. Joint Ventures

If IUS is developed through a joint venture between two or more entities, including at least one entity outside of the DoD, the DoD Component must capitalize the IUS asset if it meets the criteria for capitalization, based on its portion of the development cost in relation to the capitalization threshold. The DoD Component will only record the portion it funded which will be capitalized if it meets the criteria for capitalization.

G. Bulk Purchases of Software Applications/Programs

1. Bulk purchases must be considered if they may materially affect the fiscal year financial statements during which they were purchased. The determination of whether an item is material depends on the degree to which omitting or misstating information about the item makes it probable that the judgment of a reasonable person relying on the information would have been changed or influenced by the omission or the misstatement. To ensure that the statements are not materially affected, new bulk purchases of software with an aggregate cost that exceeds the capitalization threshold must be capitalized.

2. An exception to this requirement includes license agreements that do not meet the criteria established for capital leases in subparagraph 270204.H. Costs related to such purchases must be expensed in the period incurred.

3. When multiple acquisitions of the same IUS application(s)/programs (for example spreadsheets, word processing programs, etc.) or modules or components of a software system are made as part of a single contract within a fiscal year, the purchases must be added together to determine whether they meet the capitalization threshold. Purchases made on a single contract during separate fiscal years are to be considered separately. DoD Components must not split bulk purchases into multiple transactions with the intent of avoiding capitalization.

4. Bulk purchases of licensed IUS with terms less than two years in length do not need to be considered for capitalization. Table 27-3 provides capitalization guidelines for bulk purchase licenses.

Table 27-3. Capitalization is Dependent on Term and Aggregate Purchase Amount

Bulk Purchased License Terms	Aggregate Purchase Amount	Guidance
License Term < 2 years	N/A	Expense
License Term = / > 2 years or Perpetual	Under capitalization threshold	Expense
License Term = / > 2 years or Perpetual	Equal to or exceeding capitalization threshold*	Capitalize
*Maintenance agreements included in the purchase of licenses are not to be considered part of the cost for this determination.		

H. Software Licenses

1. Software licenses are defined as licenses for which the license holder is only entitled to use the software for a specified time period, after which the right to use the software expires and the license must be renewed or a new license purchased in order to continue using the software. License agreements to use software come in many forms and vary in length of the license period. Software licenses can be term or perpetual.

a. Term licenses provide the right to use the software for a specified period of time. The determination of whether term licensed IUS will be capitalized or not must be based on lease accounting concepts in which the criteria in Table 27-3 are applied.

b. Perpetual software licenses give the DoD Component the right to use the software in perpetuity in exchange for an upfront cost, which could be charged as a one-time payment or financed over a set period of time. If the license is perpetual, then the entity is purchasing the IUS and must apply the capitalization criteria to determine if the license must be capitalized or expensed.

2. If one of the following criteria applies, the IUS can be expensed and the lease criteria analysis does not need to be conducted:

a. The license term is less than two years;

b. The license cost (excluding any maintenance agreements) is less than the capitalization threshold; or

c. The aggregate cost of a bulk license purchase (excluding any maintenance agreements) is less than the capitalization threshold. See subparagraph 270204.G for guidance related to bulk purchases of software.

3. If none of the criteria listed in subparagraph 270204.H.2 is applicable, the capital lease criteria described in Table 27-4 must be applied. If any one or more of the criteria listed in Table 27-4 apply, the IUS must be recorded as a capital lease.

Table 27-4. Capital Lease Criteria as Applied to Licenses

Criteria	Comment
The license transfers ownership of the property to the licensee by the end of the license term.	For IUS, this would mean that the license transfers ownership of the intellectual property (e.g., source code) to the licensee by the end of the license term.
The license contains an option to purchase the software at a bargain price.	For IUS, this would mean that the license contains an option to purchase the software intellectual property (e.g., source code) at a bargain price.
The present value of minimum license payments, excluding that portion of the payments representing executory cost, equals or exceeds 90 percent of the fair value of the software.*	It is very unusual for software to meet this criteria. The value of the software itself typically far outweighs a license to use a copy of it.
The license term is equal to or greater than 75 percent of the estimated economic life of the software.*	Some licenses may meet this criteria. Economic life is defined as the estimated remaining period during which the property is expected to be economically usable by one or more users, with normal repairs and maintenance, for the purpose for which it was intended at the inception of the lease, without limitation by the lease term. For example, a perpetual license will always be equal or greater than 75 percent of the estimated economic life. A license term of 5 years for software that has an economic life of 10 years would not meet this criteria.
* The last two criteria are not applicable when the beginning of the license term falls within the last 25 percent of the total estimated economic life of the software.	

4. A license agreement may include executory costs for maintenance and technical support. DoD Component judgment should apply in determining what portions of license fees are attributable to software capitalizable costs versus executory costs. Assuming lease capitalization criteria and thresholds are met, software license capitalization amounts may be derived from the payment schedule contained in the license agreement. As stated in SFFAS 5, if the portion of the minimum lease payments representing executory cost is not determinable from the lease provisions, the amount should be estimated. DoD Components may also want to consider having each license agreement specifically identify the various costs throughout the license life cycle, for example, initial license, maintenance, and enhancement.

5. Additional guidance regarding accounting for license agreements includes:

a. Maintenance costs agreed to as part of the initial license agreement are to be expensed in the period they are incurred;

b. “True-up” costs associated with unlimited license agreements or enterprise licenses that may occur (depending on the agreement terms) at the end of each year to reconcile and account for the actual quantity of users will also be expensed; and

c. Software upgrades that are included in annual maintenance and security assurance agreements should be expensed, not be capitalized as enhancements or separate assets.

6. License agreements that do not meet the criteria established for capital leases set out in Table 27-4 must be expensed by the DoD Component in the period incurred.

I. Cloud and Other Subscription Based Services

1. A cloud computing service is any resource that is provided over the Internet. It has the following essential characteristics: on-demand self-service, broad network access, resource pooling, rapid elasticity, and measured service. The most common cloud service resources are: software as a service, platform as a service, and infrastructure as a service. Cloud services can take a number of forms. To determine whether the arrangement includes capitalized IUS, the DoD Component will need to examine the nature of the arrangement and apply the capitalization criteria.

2. When a DoD Component pays regular subscription fees to access and use software that is funded, maintained, and owned by a non-DoD entity, the subscription costs are to be expensed in the period incurred. This scenario is a service and does not constitute an IUS asset for the DoD Component.

3. A subscription arrangement using a cloud with a non-DoD entity can result in DoD-owned IUS if the using DoD Component takes possession, or has the ability to take possession of a software application without incurring a significant penalty. DoD Components must capitalize this IUS if it meets the capitalization criteria as described in subparagraphs 270204.D and 270204.E.

4. When a cloud or subscription arrangement exists between DoD Components, the Component that owns the software (see subparagraph 270204.A) will report it as IUS. The subscribing DoD Component(s) will expense any fees paid for the service in the period incurred.

5. If a cloud computing arrangement includes a software license, the customer must account for the software license element of the arrangement consistent with the acquisition of other software licenses in accordance with the lease criteria discussed in subparagraph 270204.H. SFFAS 10 is not applicable to a cloud computing arrangement that does not convey a contractual right to the IUS or to ones that do not include an IUS license. The entity that develops and owns the software, platform or infrastructure used in the cloud computing arrangement would account for the software development in accordance with SFFAS 10. If the funding to develop cloud computing is shared among entities without clear ownership, the service provider entity that receives funding and is responsible for maintaining the software, platform or infrastructure must account for the software in accordance with SFFAS 10 and the full cost/inter-entity cost requirements of SFFAS 4.

J. Shared Services

1. Shared services means a mission or support function provided by one business unit to other business units within or between organizations. The funding and resourcing of the service is shared and the providing entity effectively becomes an internal/external service provider.

2. There are three types of shared service structures in the Federal Government:

a. Intra-agency. Intra-agency shared services include those provided within the boundaries of a specific organization such as a Federal Department or Agency, to that organization's internal units. Intra-agency shared services would be those between one DoD Component and another DoD Component.

b. Inter-agency. Inter-agency shared services are those provided by one Federal Organization to other Federal Organizations that are outside of the provider's organizational boundaries. Inter-agency shared services would be those between one DoD Component and another Federal Agency/Organization outside of DoD.

c. Commercial. Commercial shared services are those provided by private vendors.

3. For intra-agency shared services, a cost allocation methodology could be developed in accordance with SFFAS 4, paragraphs 120-125. Additional guidance on cost allocation methodology can be found in the Volume 4, Chapter 19. For inter-agency shared services and commercial shared services, the service provider entity that owns (receives funding/responsible for maintaining) the software must account for the software in accordance with SFFAS 10. In the event that the entity receiving the service (the customer) has the contractual right to take possession of the software at any time during the hosting period without significant penalty, and it is feasible for the customer to either run the software on its own hardware or contract with another party unrelated to the vendor to host the software, then the customer must account for the software in accordance with SFFAS 10.

4. If the shared service arrangement includes a software license, the DoD Component must account for the software license element of the arrangement consistent with the acquisition of their other software licenses, as discussed in subparagraph 270204.H. SFFAS 10 is not applicable to a shared service arrangement that does not convey a contractual right to the IUS or to ones that do not include an IUS license.

K. Accountable Records of IUS

DoD Components must establish accountable records for all government IUS purchased or otherwise obtained. IUS which meets the criteria for capitalization must be accounted for in an APSR. IUS which does not meet the criteria for capitalization must be accounted for in either an APSR or approved managerial system. Managerial systems must contain all general data elements

that would be contained in a data compliant APSR. In addition, managerial systems must have documented controls and procedures in place that are sufficient to withstand potential audit scrutiny and support the audit requirement of a complete universe of assets. The primary Accountable Property Officer or designated delegate should grant managerial system approval. See DoDI 5000.76.

*270205. IUS Enhancements

A. An IUS enhancement is a modification to existing IUS that provides it with significant additional capabilities and enables the software to perform tasks that it was previously incapable of performing. DoD Components must capitalize an enhancement that increases the capability of the IUS when its cost meets or exceeds the capitalization threshold. Criteria to capitalize enhancements to IUS differs from that of other PP&E in that changes that merely extend the useful life or improve efficiency are to be expensed, irrespective of the cost. (Even though the costs associated with the extension of useful life are expensed, the amortization of any previously capitalized amount must be extended to reflect that new useful life period.) Capitalizable enhancements normally require new software specifications and may require a change to all or part of the existing software specifications. For example, DoD Components should capitalize the cost of modifying existing software for making ad hoc queries, if it required new software specifications and/or changes to existing software specifications and it also exceeds the capitalization threshold. In addition, the DoD Components should expense the nominal charges paid for enhanced versions of software in the period incurred.

B. If one module is dependent upon another to function, then those modules must be evaluated together as one enhancement. Components must amortize all costs of an enhancement that have been capitalized based on the IUS capitalization criteria, including any costs carried over or allocated from the original software, over the enhancements estimated useful life, which should not exceed five years.

C. DoD Components must begin accumulating costs for enhancements when it is determined that it is more likely than not that the enhancement will result in new capabilities; and the project phase in which the costs are being incurred and the nature of the cost meets the criteria for capitalization treatment set out in Table 27-1; and the estimated total cost of the enhancement meets the IUS capitalization threshold. When the development of the enhancement takes place over multiple periods, the costs will accumulate in account 183200 (Internal Use Software in Development) until the completion of the enhancement (see subparagraph 270207.C on placed-in-service dates), at which time the costs are moved to account 183000 (Internal Use Software).

D. DoD Components must separately account for enhancements in a manner that allows them to specifically identify and support each capitalized enhancement made to the IUS.

E. An enhancement to IUS that meets or exceeds the capitalization threshold to correct a design flaw, and in effect doubles its useful life, must be expensed in the period incurred, unless the enhancement adds new capabilities to the software. However, the useful life

of the IUS is subject to adjustment and must reflect the enhancement. Knowledgeable personnel must determine and document the additional useful life, which should not exceed five years added to the existing useful life.

F. The cost of minor enhancements resulting from ongoing systems maintenance or incurred solely to repair a design flaw without adding additional capabilities must be expensed in the period incurred. Examples of minor enhancements include updating data tables, web-enabling, customizing reports, or changing graphic user interfaces. Enhancements that extend the useful life of the software without adding significant capabilities are to be considered minor enhancements and expensed. However, in instances where the useful life of the software is extended, the amortization period must be adjusted as described in subparagraph 270205.E.

G. A specific software development project may include expenditures for enhancements and maintenance that cannot be easily separated but may be reasonably and consistently allocated. One approach that can be used is a ratio based on the projected work hours for development phase activities relative to other types of work. Such a ratio can be applied to determine the expenditures that should be capitalized when the expenses meet the other capitalization criteria. The basis for allocating costs must be applied consistently and in accordance with GAAP.

H. Documentation related to IUS enhancement decisions, such as the justification for capitalizing the enhancement, a change of useful life, and the amount capitalized must be retained. Specific documents that support these decisions can vary by organization and asset, but could include an analysis from software developers or a cross-functional review team that defines the enhancement's impact on functionality and useful life.

I. The cost of enhancements to more than one IUS asset as identified by a unique identifier, when performed under a single contract or work order that cannot be specifically identified by asset must be capitalized only if the allocated cost per IUS equals or exceeds the appropriate DoD capitalization threshold and the enhancements are determined more likely than not to add additional capability to the existing software.

J. When a single IUS goes under more than one enhancement and the enhancements are part of one overall effort to increase the software's functionality, and/or useful life; the sum of the costs of the enhancements must be capitalized, if the summed costs equal or exceed the appropriate DoD capitalization threshold. This is required even when the enhancements are funded separately. The enhancements must be capitalized when the determination has been made that it is more likely than not that the enhancements will result in new significant capabilities.

*270206. Maintenance and Repair

A. Maintenance and repair costs are not considered capital enhancements, regardless of whether the cost equals or exceeds DoD capitalization threshold. Maintenance and repairs are activities directed toward keeping IUS asset in an acceptable condition so that it continues to provide services and achieves its expected useful life. Maintenance and repair

activities include subsequent security accreditations (not included in user acceptance testing); software diagnostics; repair processing and/or performance failures; updates to documentation; minor software updates; minor corrections to design flaws; and other activities needed to preserve or maintain the software. Maintenance and repairs, as distinguished from enhancements, exclude activities directed towards expanding the capacity of IUS or otherwise upgrading it to serve needs different from, or significantly greater than, its current use.

B. The costs of maintenance agreements purchased with a software license are not included in the historical cost of IUS when determining whether to capitalize the IUS. If maintenance costs are not distinguishable from the cost of the license itself, reasonable and documented estimating methods must be used. Upgrades that are included in annual maintenance and security assurance agreements will not be capitalized as enhancements or separate assets.

*270207. Amortization

A. Amortization is the systematic and rational allocation of the acquisition cost of IUS, over its estimated useful life. The DoD recovery periods (useful life) for IUS amortizable assets are set out in Table 27-5. The useful life must be determined during the planning phase of the software development, based on the length of time it is expected to have economic benefit or service potential to the DoD Component. The decision on the useful life must be documented and made with input from personnel familiar with the software's technical characteristics and planned use. Software acquired for research and development with no alternative future use will be amortized over the period of the project as opposed to the normal life-cycle amortization.

B. The recorded cost of IUS and enhancements to IUS, which have been capitalized according to the guidance in Table 27-1, must be amortized. Such capitalized amounts, as well as associated amounts of accumulated amortization and amortization expense, must be reflected in DoD Component's financial statements.

C. DoD Components must document the placed-in-service dates for both acquired IUS and developed IUS. Documented placed-in-service dates are critical in determining when to start amortization of capitalized IUS costs. IUS is considered placed-in-service when final technical acceptance testing is completed. The point at which this milestone is reached can vary for different types of software acquisitions.

1. For IUS acquired through a Major Automated Information System acquisition program, the Full Deployment Decision date made by the Milestone Decision Authority will serve as the placed-in-service date.

2. For other IUS system acquisitions, the Initial Operational Capability (IOC) date will be used as the placed-in-service date. System's Capability Development Document (CDD) and/or Capability Production Document (CPD) often define the IOC. DoD Components can use other supporting documents for acquisitions that do not require a CDD or CPD.

3. If knowledgeable parties within a DoD Component determine that a placed-in-service date other than the ones listed in subparagraphs 270207.C.1 and C.2 better align to the completion of final technical acceptance testing for a specific software acquisition, the alternate placed-in-service date can be used. However, the DoD Components must document and justify the decision.

D. Before beginning amortization, the IUS must have successfully completed final acceptance testing. This criteria is necessary, especially for internally developed software but also for contractor-developed and COTS software because testing plays a major role for software assets by demonstrating that the software product can meet the requirements and of the need for a clear point for ending the developmental phase.

E. When IUS is replaced with new software, the unamortized cost of the old software must be expensed when the new software successfully completes testing. No adjustments will be made to the previously recorded amortization. Any additions to the book value or changes in useful life must be treated prospectively. The change should be accounted for during the period of the change and future periods.

F. All IUS must be accounted for in an APSR. Figure 27-2 provides a decision tree to assist in determining what elements of an IUS project should be capitalized for financial reporting purposes.

G. Proper supporting documentation must be retained by the program office to justify the estimated useful life of the program. Examples of proper documentation are engineering estimates, operational requirements documents, mission needs statements, commercial industry-equivalent information, contracts, and acquisition documents (such as the Select Acquisition Report). See paragraph 270302 for additional information on supporting documentation requirements.

H. In the case of IUS assets, after the successful completion of the final technical acceptance testing described in subparagraph 270270.D, the event that triggers the calculation of amortization is the date the asset is installed and placed-in-service (regardless of whether it is actually used). In the case of internally developed IUS, the costs of developing the IUS that are capitalizable should be recorded in the Internal Use Software in Development account (183200) but are not amortized until the software is placed-in-service, at which time the balance (total capitalizable development costs) should be transferred to the Internal Use Software account (183000). Amortization should begin when a module or component has been successfully tested. If the use of a module is dependent on the completion of another module(s), the movement from account 183200 to account 183000 will take place and amortization will begin when both that module and the other module(s) have successfully completed testing and are placed-in-service.

I. DoD policy permits the use of only the straight-line method of amortization. Straight-line amortization expense is calculated based on the recorded cost divided equally among accounting periods during the software's useful life based on recovery periods in Table 27-5. The salvage value for all capitalized IUS for the DoD Components should be zero.

J. If an IUS asset remains in use longer than its estimated useful life, it must be retained in the APSR, as well as the accounting records, and reflect both its recorded cost and accumulated amortization until disposition of the software.

K. WCF activities are required to recognize and amortize IUS assets in accordance with the guidance in this chapter without regard to whether such assets are procured through a WCF activity's Capital Purchase/Investment Program budget or whether amortization for such assets is included in rates charged to customers. The recognition of IUS assets and the amortization of such assets by WCF activities therefore may be different for financial statement reporting purposes than the amortization amounts used for WCF rate development and budget presentation. All IUS asset amortization of WCF activities must be recognized as an expense on the Statement of Net Cost, reflected in the Statement of Changes in Net Position, included in accumulated amortization amounts on the Balance Sheet, and reported in the "Defense Working Capital Fund Accounting Report [Accounting Report (Monthly) 1307] (AR(M)1307)." Accounting Report 1307 is described in Volume 6a Chapter 15. Amortization recorded on IUS assets that was not acquired nor will be replaced through use of Defense WCF resources must be classified as non-recoverable for rate setting purposes and reported appropriately on the AR(M)1307. Defense WCF rates charged to customers are based on guidance in Volume 2B and Volume 11B.

Table 27-5. DoD Recovery Periods for Amortizable IUS Assets

DOD RECOVERY PERIODS FOR AMORTIZABLE IUS ASSETS (IUS is capitalized only if it meets the capitalization threshold)	
Description of IUS Assets	Recovery Period
Capitalized IUS	2, 3, 4, 5 or 10 Years*
Licenses	Term of the license agreement
Perpetual Licenses	5 Years
IUS Upgrades	Not capitalized**
Enhancements	Not more than 5 years***
* The useful life will be determined during the planning phase of the asset's development based on the length of time it is expected to have economic benefit or service potential to the DoD Component.	
** The amortization period of an IUS must be adjusted (not extending more than 5 years) if minor upgrades resulting from ongoing systems maintenance or repair of a design flaw extend the useful life of the software without adding additional capabilities. The cost of the upgrades should be expensed in the period incurred. Also note the upgrades that do add additional capabilities would be considered enhancements and would be capitalized and amortized if they meet the capitalization criteria in subparagraph 270204.E.	
***See paragraph 270205 on the criteria for capitalizing versus expensing of IUS enhancements.	

*270208. Impairment

A. Impairment **must** be recognized and measured when one of the following occurs and is related to post-implementation/operational software:

1. The software is no longer expected to provide substantive service potential and will be removed from service; or

2. A significant reduction occurs in the **software's or software module's** capabilities, functions, or uses.

B. If the impaired software is to remain in use, the loss due to impairment **must** be measured as the difference between the book value and either:

1. The cost to acquire software that would perform similar remaining functions (i.e., the unimpaired functions) or, if that is not feasible;

2. The portion of the book value attributable to the remaining functional elements of the software.

C. **The loss must be recognized upon impairment, and the book value of the asset reduced accordingly. If neither criteria listed in subparagraph 270208.B can be determined, the DoD Component should continue to amortize the book value over the remaining useful life of the software. However, this decision and associated analyses must be documented and retained.**

D. If the impaired software is to be removed from use, the loss due to impairment **must** be measured as the difference between the book value and the NRV, if any. The loss **must** be recognized upon impairment, and the book value of the asset reduced accordingly. The NRV, if any, **must** be transferred to an appropriate asset account until the software is disposed of and the amount is realized.

E. When it is more likely than not that a developmental software project will not be completed, no further costs are to be capitalized and any costs that have been capitalized must be **expensed**. Indications that the software development may no longer be completed include:

1. **The expenditures are neither budgeted nor incurred to fund further development;**

2. **The discontinuance of the business segment for which the software was designed;**

3. **The inability to resolve programming difficulties timely;**

4. A decision to obtain COTS software instead and abandon the current software development; or

5. Major cost overruns occur.

F. When a developmental software project is suspended pending management's evaluation as to whether to resume or terminate the project, the software development cost may remain capitalized in an Internal Use Software in Development account (USSGL 183200) as long as it is more likely than not that the developmental software project will eventually be completed and the cost incurred or expected to be incurred meets the capitalization threshold. The status of the project must be reevaluated periodically and the capitalized cost must be written off if management concludes that it is more likely than not that the software will not be placed-in-service in the future.

G. The loss from impairment, if any, must be recognized and reported in the Statement of Net Cost in the period in which the DoD Component concludes that the impairment is both (1) a significant decline in service utility and (2) expected to be permanent. Such losses may be included in program costs or costs not assigned to programs. A general description of the IUS for which an impairment loss is recognized, the nature (e.g., damage or obsolescence) and amount of the impairment and the financial statement classification of the impairment loss must be disclosed in the notes to the financial statements in the period the impairment loss is recognized if the amount is significant to the financial statements.

H. The impairment loss must be reported net of any associated recovery of the net realizable value when the recovery and loss occur in the same fiscal year. Recoveries reported in subsequent fiscal years must be reported as revenue or other financing source as appropriate. The amount and financial statement classification of recoveries must be disclosed in the notes to the financial statements.

I. The costs incurred to replace or restore the lost service utility of impaired IUS remaining in use must be accounted for in accordance with applicable standards (i.e., recognized according to the nature of the costs incurred and the appropriate capitalization threshold).

*270209. Removal/Disposal

A. In TR 14, FASAB defines removal from service as an event that terminates the use of a General PP&E asset. Removal from service may occur because of a change in the manner or duration of use, change in technology or obsolescence, damage by natural disaster, or identification as excess to mission needs. Removal from service must be considered other than permanent unless (1) the asset's use is terminated and (2) there is documented evidence of the DoD Component's decision to permanently remove the asset from service. If only one of the two business events has occurred, permanent removal from service has not occurred (i.e., the removal is considered other than permanent).

B. If an IUS's normal use is terminated (i.e., it no longer provides service in the operations of the entity) but the DoD Component has not yet decided to permanently remove the IUS from service, the removal from service is considered other than permanent. Other than permanent removal from service is evidenced by activities such as continuing low-level maintenance to sustain the IUS in a recoverable status or until reutilization efforts are exhausted. For example, IUS taken out of service on a temporary basis is considered other than permanently removed from service. In such cases, the recorded cost of the IUS will remain in the Internal Use Software account (USSGL 183000). There is no change in the reported value for IUS that have been other than permanently removed from service and the IUS must continue to be amortized. Amortization charges to expense for IUS will continue to be recorded in USSGL 183900.

C. If (1) an IUS's use is terminated and (2) the DoD Component has documented its decision to permanently remove the IUS from service, the removal from service must be accounted for as permanent. Permanent removal from service is evident from the DoD Component's documented decision to dispose of an IUS by selling, recycling, or donating the IUS. The recorded cost as well as the accumulated amortization of an IUS permanently removed from service must be removed from the accounts in which they are reported, and the IUS must be recorded at its NRV in a General Property, Plant and Equipment Permanently Removed But Not Yet Disposed account (USSGL 199500). USSGL account 199500 is defined in the DoD Standard Reporting [Chart of Accounts](#) under the DoD Account Definitions tab as the NRV of General PP&E that is permanently removed from service but not yet disposed and is reclassified in accordance with FASAB TR 14, paragraphs 10 and 12. NRV is the estimated amount that can be recovered from disposing of the asset less estimated costs of completion, holding, and disposal. Any difference between the net book value of the asset and its expected NRV must be recognized as a gain or loss. Any gain should be recorded in the Gains on Disposition of Assets – Other account (USSGL 711000); any loss should be recorded in the Losses on Disposition of Assets – Other account (USSGL 721000). The expected NRV should be evaluated at the end of each fiscal year and any change in NRV should be recognized as a gain or loss. IUS permanently removed from service is no longer amortized.

D. When an IUS is disposed of (e.g., by selling, recycling, donating, or destruction) the IUS must be written off from the financial records and financial statements and the difference between any disposal proceeds and the IUS's net book value must be recognized as a gain or loss as described in subparagraph 270209.C. In such case, if the DoD Component receives a consideration (e.g., cash) for the disposal, a receipt of cash should be recorded in the Fund Balance with Treasury account (USSGL 101000). If the funds (consideration received) are not apportioned to the DoD Component, the fund must be transferred to miscellaneous receipts of the Treasury. There will be no consideration received for a donation. The disposal start date is the calendar date of a legally enforceable and recognizable obligation to complete the disposal action. For transfers and sales, this represents the date on which the instrument is endorsed or operation is ceased, whichever comes later. For natural disasters, this represents the actual date of the incident.

2703 ADDITIONAL CONSIDERATIONS

*270301. Use of Canceled Treasury Account Symbol

A. The Department of Treasury's Governmentwide Treasury Account Symbol Adjusted Trial Balance System (GTAS) is a data collection system that replaces the reporting functionalities of Federal Agencies Centralized Trial-Balance System I and II, Intragovernmental Fiduciary Confirmation System and Intragovernmental Reporting and Analysis System as the primary means for DoD Components to report their trial balance data to the Department of Treasury. Capitalized assets are required to be reported and remain in GTAS after the original purchasing Treasury Account Symbol (TAS) has expired and been canceled. If a capitalized asset has not been moved to a "C" TAS as described in 270301.B. GTAS will provide a "C" TAS on the GTAS Super Master Account File (SMAF) for each fund family represented on the SMAF. The system generated "C" TAS will have three components: the three digit agency identifier, availability type "C", and a four digit main account.

B. All DoD Components must use the "C" availability type TAS to report capitalized assets. Assets may be moved to a C TAS at any time from the purchase date to the date the original purchasing fund cancels. (Refer to the [TFM, Part 2, Chapter 4700](#) for additional information.)

C. To transfer an asset to a C TAS:

1. Use USSGL account transaction E510 to transfer-out the asset from the purchasing fund account.

2. Use USSGL account transaction E606 to transfer-in the asset into the appropriate C TAS.

270302. Supporting Documentation

Entries to record financial transactions in accounting system general ledger accounts and/or the supporting subsidiary accountable property records and/or systems must:

A. Be supported by source documents that reflect all transactions affecting the DoD Component's investment in the IUS.

1. All acquisitions, whether by purchase, transfer from other agencies, donation, or other means, **must be supported** as of the date the DoD Component takes custody of the IUS. The documents listed in Table 27-6, where applicable, **must** be readily available to support the changes in asset value or physical attributes as a result of new acquisition or capital enhancement.

Table 27-6. Supporting Documentation for IUS Acquisition

Evidence	Examples
Unique Identification	Assignment of unique identifier
Project Approval	Such as, but not limited to, a Work Order
Obligation on Behalf of the Government	Such as, but not limited to: <ol style="list-style-type: none"> 1. For contracts, contract modifications, or change orders: <ul style="list-style-type: none"> • Statement of Work; • Dollar Amount of Contract; • Location; • Source of Funds; • Parties to the Contract; and • Signature Page [Signature of All Parties]. 2. Documentation of labor hours; 3. Approved Work Order.
Payment Submitted	Such as, but not limited to: <ol style="list-style-type: none"> 1. Approved last invoice reflecting the total amount submitted for payment and received to date; 2. Evidence of in-house development costs, including labor; 3. Indirect Costs incurred internally by the gaining activity that relate to the new acquisition or capital enhancement.
Acceptance	Such as, but not limited to: <ol style="list-style-type: none"> 1. DoD (DD) Form 250, Material Inspection and Receiving Report; 2. Executed acquisition document and appraisal results for the donated IUS; 3. Signed agreement for software licenses; 4. A signoff document confirming key development milestones such as technical acceptance tests are met; 5. Documents to support the amount that has been expensed versus capitalized during the software development phase. 6. Executed reversionary document; and 7. Transfer letter and documents for transferred assets.

2. All disposals or retirements [must be supported as of the date](#) the IUS leaves the custody of the DoD Component to provide an adequate audit trail for the disposal of [an](#) asset. The execution of certain disposal events will generate financial or administrative accountability transactions. [These documents, where applicable, must be readily available to support disposals:](#)

- a. 'Declaration of excess' document;
- b. Approval documentation [for the disposal](#);
- c. Original acquisition documents;
- d. Legal instruments (such as a [license agreement](#) or contract) to indicate legal obligation to dispose of an asset;
- e. Document showing the disposal start date;

f. Receipt documentation; and

g. Transfer documents for transferred assets or as otherwise stated.

3. Documents that support the recorded cost of IUS assets must be retained by the DoD Component in accordance with the requirements contained in Volume 1, Chapter 9 or as otherwise stated. Documentation (original documents and/or hard and electronic copies of original documentation) must be maintained in a readily available location during the applicable retention period to permit the validation of information pertaining to the asset such as the purchase cost, purchase date, and cost of enhancements. The documentation must also be linked to the appropriate unique identifier(s). Supporting documentation may include, but is not limited to, the documentation as outlined in this subparagraph. DoD Component asset managers will maintain all applicable documentation for the retention period outlined in Volume 1, Chapter 9.

B. Include sufficient information indicating the quantity (as applicable would include the number of seats for which the IUS asset is loaded; the number of licenses; and/or the number of copies of a computer disk purchased), location and unit cost (as measured consistently with the criteria for quantification) of the IUS. The accountable property records must be designed to be of maximum assistance in making procurement and utilization decisions, including decisions related to identifying potential excess IUS that may be available for reuse, transfer to other DoD Components, or made available for disposal in accordance with current DoD regulations and other regulatory requirements.

C. Identify and classify IUS that was capitalized, recorded in the APSR and accounting system, and reported in the financial statements.

D. Be based on the same documents, to ensure that entries to the accounting and accountable property records are the same. This will ensure that the property accountability records are integrated and subsidiary to the accounting system and those records can be reconciled with the accounting system.

E. Include documents used to accumulate the cost of developmental projects. Each document must link to the appropriate asset unique identifier. For a listing of those costs that may be incurred during the development, see Table 27-1.

F. Include all IUS possessed by the Department (to include property held by others) and IUS of others held by DoD through seizure, forfeiture, loss, or abandonment.

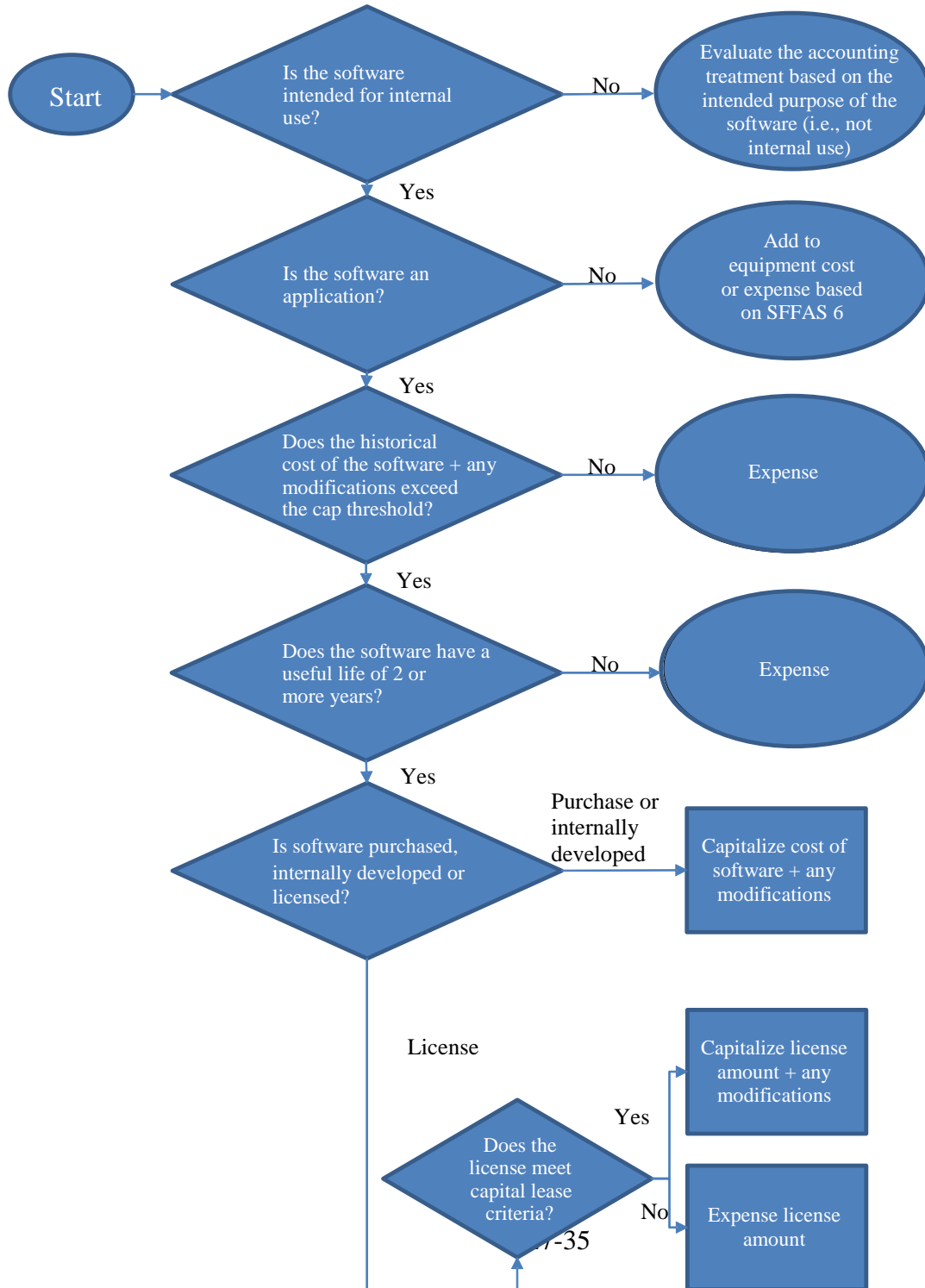
G. Provide information to identify and account for licenses, regardless of whether the license meets the capital lease criteria or whether the value of the licenses exceeds DoD capitalization thresholds.

H. Provide information to identify and account for capitalized enhancements to IUS.

*270303. Reporting Requirements

DoD Components with IUS should reference a note on the Balance Sheet that discloses information about the reported IUS assets. See Volume 6B, Chapter 10 for the specific reporting requirements.

*Figure 27-2. Capitalization Decision Tree for IUS Purchased from Commercial Off-the-Shelf Vendors; IUS Internally Developed by DoD and IUS Developed by a Third Party on Behalf of DoD



*Annex 1. Definitions and Examples

The following table contains common terms as they are generally defined by information technology and software programming professionals. It also includes scenarios relevant to IUS.

Definition	Classified as IUS?	Capitalization	DoD Examples*
Access Control Software			
This type of software, which is external to the operating system, provides a means of specifying who has access to a system and the specific capabilities authorized users are granted.	No	Include with equipment costs	CA-ACF2, RACF
Application Software			
A software program that performs a specific function directly for a user and can be executed without access to system control, monitoring, or administrative privileges.	Yes	Yes - When capitalization criteria is met	Microsoft Excel, Adobe Photoshop
Cloud – Public			
A cloud based environment that is generally external to the Department with infrastructure owned and managed by a third party. Public cloud services are generally subscription based.	No	No	Dropbox
Cloud – Private			
A cloud based environment that is generally internal to the Department and used solely by DoD Components.	Yes	Yes – When the capitalization criteria is met, the DoD Component that controls the IUS has financial reporting responsibility	DISA milCloud
Database Management System (DBMS)			
Computer software applications that interact with the user, other applications, and the database itself to capture and analyze data.	Yes	Yes - When capitalization criteria is met	Oracle Enterprise Manager

Definition	Classified as IUS?	Capitalization	DoD Examples*
Enterprise Resource Planning System			
Commercial software that integrates business information flowing through the Component. ERP systems contain functional modules (e.g., financial, accounting, human resources, supply chain, and customer information) that are integrated within the core system or interfaced to external systems.	Yes – portions of ERP systems are IUS (excluding any hardware acquired as part of the system)	Yes – portions of ERP systems are capitalized	Navy ERP, GFEBBS, LMP, DAI
Firmware			
A program recorded in permanent or semi-permanent computer memory.	No – may be capitalized as part of equipment	May be capitalized a part of equipment	Radar system software, lathe
Freeware / Open Source Software (OSS)			
Software that is offered at no cost.	No	No	Internet browser
Hardware			
The physical components of IT, including the computers, peripheral devices such as printers, disks, and scanners, and cables, switches, and other IT equipment.	No	May be capitalized as general equipment depending on applicable capitalization criteria being met	Router, Server, Modem, Switch
License – Annual			
A software license that must be renewed annually to continue using the software.	Yes	No - an annual license does not meet the useful life criteria of 2 years for capitalization	Microsoft Lync, VMWARE vSphere
License – Enterprise			
A license that allows use of the software throughout an organization or for a specified number of users.	Yes	Only if it meets capitalization threshold and capital lease criteria	Microsoft Office, Oracle
License – Perpetual			
A software license that gives the Department the right to use the software in perpetuity.	Yes	Only if it meets capitalization threshold	SAP Chrystal Reports

Definition	Classified as IUS?	Capitalization	DoD Examples*
Middleware			
Computer software that provides services to software applications beyond those available from the operating system.	Yes	Yes - If the system it is part of meets capital criteria	Linux Kernel
Portal			
Web-based application that provides personalization, single sign-on, and content aggregation from different sources, and hosts the presentation layer of information systems.	Yes	Yes – When capitalization criteria is met	Audit Response Center (ARC) Tool
Simulation Software			
Based on the process of modeling a real or proposed system with a set of mathematical formulas that allows the user to observe an operation before performing it.	Yes	Yes – When capitalization criteria is met	F-35 Lightning II Training Software
Operating System			
The software that controls the execution of other computer programs, schedules tasks, allocates storage, manages the interface to peripheral hardware, and presents a default interface to the user when no application program is running.	No	Include in equipment costs	Windows, Linux
System / IT System			
The term “system” by itself is not limited to any specific resource. A system may be any two resources that work together to produce a specific outcome. Internal use software may or may not be one component of an overall “system”.	Yes – software components of a system or IT system are IUS	Yes - When capitalization criteria is met	Navy ERP, GFEBs, DAI, CAMIS, MC4
Utility Program			
System software designed to perform a particular function or system maintenance.	No	Include in equipment costs	CD burner, Disk defragmenter, virus scan
Web Application			
An application that is accessed via the web over a network.	Yes (assuming it is owned by a DoD Component)	Yes - When capitalization criteria is met	Outlook Webmail

*DoD examples provided may or may not be capitalized

*Annex 2. Alternative Valuation Methodology for Establishing Opening Balances for Internal Use Software

A20101. Establishing Opening Balances for Internal Use Software

A. The alternative valuation method for establishing opening balances for Internal Use Software (IUS) described in Federal Accounting Standards Advisory Board (FASAB) Statement of Federal Financial Accounting Standards (SFFAS) 50, “Establishing Opening Balances for General Property, Plant and Equipment: Amending Statement of Federal Financial Accounting Standards (SFFAS) 6, SFFAS 10, SFFAS 23, and Rescinding SFFAS 35” is available only once to each reporting entity. Therefore, prior to the establishment of IUS opening balances, DoD Components must validate that they are prepared to account for and comply with the recognition, measurement, presentation and disclosure requirements for IUS in accordance with FASAB SFFAS 10, “Accounting for Internal Use Software.”

B. DoD Components must identify any IUS that they have capitalized prior to establishing opening balances, including capitalized development costs. All DoD Components that have not previously undergone a financial statement audit where they received an unmodified (i.e., “clean”) audit opinion will exclude the value of all IUS, including development costs, from opening balances of General Property, Plant, and Equipment on their Balance Sheet. This means that DoD Components who have not undergone a financial statement audit where they received a “clean” audit opinion will adjust their capitalized IUS, including development costs, opening balances to zero. A DoD Component that has received a “clean” audit opinion should continue to account for IUS, including development costs, in accordance with FASAB SFFAS 10 and will not reduce their balances to zero.

C. Entries in the DoD Component accounting systems/records to record IUS opening balances at zero are subject to the reporting requirements under paragraph 13 of FASAB SFFAS 21, “Reporting Corrections of Errors and Changes in Accounting Principles, Amendment of SFFAS 7, Accounting for Revenue and Other Financing Sources”. Accordingly, the entries will be reflected as a change in accounting principle. Any adjustments must be properly documented and supported to assist ongoing audit efforts.

A20102. Financial Statement Disclosure Requirements

DoD Components who adjust their opening IUS balances, including development costs, in accordance with subparagraphs A.20101.B and A.20101.C, must disclose in their financial statements that an alternative valuation method was applied in establishing their opening balances. This disclosure must describe the alternative valuation method used in the first reporting period in which the reporting entity makes an unreserved assertion that its financial statements, or one or more line items, are presented fairly in accordance with Generally Accepted Accounting Principles. An unreserved assertion is an unconditional statement.

A20103. Prospective Accounting for Internal Use Software

A. Once the opening balances for IUS have been recorded at zero as described in paragraph A.20101.B, the DoD Components shall capitalize IUS costs for IUS placed-in-service and IUS in development in accordance with the provisions of FASAB SFFAS 10 for which guidance is provided in Chapter 27. This capitalization requirement includes IUS development costs incurred after the establishment of opening balances for projects started prior to the establishment of opening balances. The DoD Components must have sufficient source documentation to support the capitalized amounts of IUS based on actual historical cost. The DoD Components must apply the provisions of FASAB SFFAS 10 regarding amortization and impairment to any unamortized capitalized cost of the IUS.

B. The DoD Components should also fully implement the systems, internal controls, processes and procedures to be compliant with accounting for IUS under FASAB SFFAS 10. They must also periodically review and update the documentation of the systems, processes, and procedures as needed.