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June 19, 2009

Mr. Russell Golden
Technical Director
Financial Accounting Standards Board
401 Merritt 7
Norwalk, CT 06856-5116

Re: File Reference No. 1660-100

Dear Russ:

Microsoft appreciates the opportunity to respond to the Discussion Paper (DP), “Preliminary Views on Revenue Recognition in Contracts with Customers”. In general, we agree with the Boards’ proposal to develop a single revenue recognition model. However, we found it difficult to respond to the DP given all of the topics not covered as listed in Appendix C. We have specific comments in the areas of the identification and satisfaction of performance obligations, standard warranties, rights of return, and sales incentives.

Identification and Satisfaction of Performance Obligations

Microsoft is concerned that the proposed model could result in an onerous exercise to identify and account for numerous performance obligations. As indicated in the DP, even a simple contract can comprise many performance obligations. While the DP provides that an entity can account for promised assets as a single performance obligation if it transfers a bundle of goods and services to a customer at the same time, software arrangements often include numerous obligations which will be satisfied at indeterminate times in the future, such as software support, “when-and-if-available” software deliverables, deployment planning services, training, etc.

We also believe the DP needs to provide more guidance on the recognition pattern for the satisfaction of certain performance obligations. For instance, we think of a “when-and-if-available” software deliverable as a stand ready obligation that is satisfied continuously over time such that ratable revenue recognition is appropriate, however, it is not clear to us whether this is a correct interpretation based on the guidance in the DP.

Further complicating the matter is the DP’s guidance concerning the allocation of the transaction price to separate performance obligations. This is highlighted in Example 2 of the DP which illustrates a software arrangement that includes two years of software support. The example indicates that the obligation to provide software support is satisfied continuously. However, in allocating the transaction price to the software support, the example assumes different estimated hours of support for each year, resulting in different revenue recognition for the support services in year 1 versus year 2.

Furthermore, this example completely ignores the reality of interim reporting requirements and the possibility of different revenue recognition for the support services in each of the four quarters of each year. Microsoft strongly believes examples such as this will unnecessarily complicate the proposed model and create onerous requirements to account for arrangements that include numerous performance obligations. We question whether the relevance and decision usefulness of this information exceeds the costs of these onerous requirements, especially when taking into account the amount of judgment that will need to be applied in allocating the transaction price based on items such as estimated hours of support for each quarter over a two year period.

Additionally, we are unsure how this interacts with the guidance in the DP that an entity can account for promised assets as a single performance obligation if it transfers a bundle of goods and services to a customer at the same time. For instance, let's add an additional performance obligation to provide training in Example 2 and assume that, similar to the software support, the obligation to provide training is satisfied continuously. Since both the obligations to provide software support and training are satisfied continuously, can they be combined? Would the expected hours of training in each quarter of each year need to be separately estimated?

Standard Warranties

Microsoft does not believe that a standard warranty should be considered a performance obligation, as we strongly believe that the purpose of a standard warranty is to ensure that the product sold functions as intended at the date of sale. Rather than being a *postdelivery service*, a standard warranty is provided to make sure a product functions as promised.

Rights of Return

Similarly, we do not believe standard rights of return are performance obligations and agree with the view that a standard return right represents a failed sale. As noted in the DP, one way of identifying a standard right of return could be whether a customer had to pay additional consideration in relation to other customers for the right of return.

Sales Incentives

We do not believe certain sales incentives on future transactions should be considered a performance obligation. While it will require some judgment, Microsoft believes that "normal" or "customary" sales incentives do not meet the definition of a performance obligation, as the entity is not transferring a future benefit to a particular customer that is not available to others in the future.

Our responses to the discussion questions raised in the DP are attached. If you have any questions, please contact me at (425) 703-6094.

Sincerely,

Bob Laux
Senior Director, Financial Accounting and Reporting

Attachment

Question 1— *Do you agree with the Boards’ proposal to base a single revenue recognition principle on changes in an entity’s contract asset or contract liability? Why or why not? If not, how would you address the inconsistency in existing standards that arises from having different revenue recognition principles?*

Response: In general, we agree with the Boards’ proposal to develop a single revenue recognition model. However, we found it difficult to respond to the DP given all of the topics not covered as listed in Appendix C. Additionally, we found it easier to focus on changes in performance obligations when thinking about the revenue recognition principle and that the discussion of changes in contract assets and contract liabilities confused the matter. As a suggestion, we would propose that the future Exposure Draft focus on the identification and satisfaction of performance obligations and that discussions focusing on assets and liabilities and what constitutes a contract be included in the Basis for Conclusions.

Question 2— *Are there any types of contracts for which the Boards’ proposed principle would not provide decision-useful information? Please provide examples and explain why. What alternative principle do you think is more useful in those examples?*

Response: Subject to the detailed comments in our response, we are not aware of any types of contracts for which the Boards’ proposed principle would not provide decision-useful information for Microsoft.

Question 3— *Do you agree with the Boards’ definition of a contract? Why or why not? Please provide examples of jurisdictions or circumstances in which it would be difficult to apply that definition.*

Response: As stated above, we found it easier to focus on changes in performance obligations when thinking about the revenue recognition principle and that the discussion of changes in contract assets and contract liabilities confused the matter. We propose that the future Exposure Draft focus on the identification and satisfaction of performance obligations and that the discussions on assets and liabilities and what constitutes a contract be included in the Basis for Conclusions.

Question 4— *Do you think the Boards’ proposed definition of a performance obligation would help entities to identify consistently the deliverables in (or components of) a contract? Why or why not? If not, please provide examples of circumstances in which applying the proposed definition would inappropriately identify or omit deliverables in (or components of) the contract.*

Question 5— *Do you agree that an entity should separate the performance obligations in a contract on the basis of when the entity transfers the promised assets to the customer? Why or why not? If not, what principle would you specify for separating performance obligations?*

Response (Questions 4 and 5): Microsoft is concerned that the proposed model could result in an onerous exercise to identify and account for numerous performance obligations. As indicated in the DP, even a simple contract can comprise many performance obligations. While the DP provides that an entity can account for promised assets as a single performance obligation if it transfers a bundle of goods and services to a customer at the same time, software arrangements often include numerous obligations which will be satisfied at indeterminate times in the future, such as software support, “when-and-if-available” software deliverables, deployment planning services, training, etc.

Further complicating the matter is the DP’s guidance concerning the allocation of the transaction price to separate performance obligations. This is highlighted in Example 2 of the DP which illustrates a software arrangement that includes two years of software support. The example indicates that the obligation to provide software support is satisfied continuously. However, in allocating the transaction price to the software support, the example assumes different estimated hours of support for each year, resulting in different revenue recognition for the support services in year 1 versus year 2.

Furthermore, this example completely ignores the reality of interim reporting requirements and the possibility of different revenue recognition for the support services in each of the four quarters of each year. Microsoft strongly believes examples such as this will unnecessarily complicate the proposed model and create onerous requirements to account for arrangements that include numerous performance obligations. We question whether the relevance and decision usefulness of this information exceeds the costs of these onerous requirements, especially when taking into account the amount of judgment that will need to be applied in allocating the transaction price based on items such as estimated hours of support for each quarter over a two year period.

Additionally, we are unsure how this interacts with the guidance in the DP that an entity can account for promised assets as a single performance obligation if it transfers a bundle of goods and services to a customer at the same time. For instance, let’s add an additional performance obligation to provide training in Example 2 and assume that, similar to the software support, the obligation to provide training is satisfied continuously. Since both the obligations to provide software support and training are satisfied continuously, can they be combined? Would the expected hours of training in each quarter of each year need to be separately estimated?

Question 6— Do you think that an entity’s obligation to accept a returned good and refund the customer’s consideration is a performance obligation? Why or why not?

Response: Similar to a standard warranty, we do not believe standard rights of return are performance obligations and agree with the view that a standard return right represents a failed sale. As noted in the DP, one way of identifying a standard right of return could be whether a customer had to pay additional consideration in relation to other customers for the right of return.

Question 7— *Do you think that sales incentives (for example, discounts on future sales, customer loyalty points, and “free” goods and services) give rise to performance obligations if they are provided in a contract with a customer? Why or why not?*

Response: We do not believe certain sales incentives on future transactions should be considered a performance obligation. While it will require some judgment, Microsoft believes that “normal” or “customary” sales incentives do not meet the definition of a performance obligation, as the entity is not transferring a future benefit to a particular customer that is not available to others in the future.

Question 8— *Do you agree that an entity transfers an asset to a customer (and satisfies a performance obligation) when the customer controls the promised good or when the customer receives the promised service? Why or why not? If not, please suggest an alternative for determining when a promised good or service is transferred.*

Question 9— *The Boards propose that an entity should recognize revenue only when a performance obligation is satisfied. Are there contracts for which that proposal would not provide decision-useful information? If so, please provide examples.*

Response (Questions 8 and 9): Microsoft believes the DP needs to provide more guidance on the recognition pattern for the satisfaction of certain performance obligations. For instance, we think of a “when-and-if-available” software deliverable as a stand ready obligation that is satisfied continuously over time such that ratable revenue recognition is appropriate, however, it is not clear to us whether this is a correct interpretation based on the guidance in the DP.

Question 10— *In the Boards’ proposed model, performance obligations are measured initially at the original transaction price. Subsequently, the measurement of a performance obligation is updated only if it is deemed onerous.*

(a) Do you agree that performance obligations should be measured initially at the transaction price? Why or why not?

(b) Do you agree that a performance obligation should be deemed onerous and remeasured to the entity’s expected cost of satisfying the performance obligation if that cost exceeds the carrying amount of the performance obligation? Why or why not?

(c) Do you think that there are some performance obligations for which the proposed measurement approach would not provide decision-useful information at each financial statement date? Why or why not? If so, what characteristic of the obligations makes that approach unsuitable? Please provide examples.

(d) Do you think that some performance obligations in a revenue recognition standard should be subject to another measurement approach? Why or why not? If so, please provide examples and describe the measurement approach you would use.

Response: We agree that performance obligations should be measured initially at the transaction price. While an argument could be made that contracts should not be remeasured even if they are deemed onerous given the Boards' rejection of a current exit price approach, Microsoft believes that a performance obligation should be deemed onerous and remeasured to the entity's expected cost of satisfying the performance obligation if that cost exceeds the carrying amount of the performance obligation.

Question 11— *The Boards propose that an entity should allocate the transaction price at contract inception to the performance obligations. Therefore, any amounts that an entity charges customers to recover any costs of obtaining the contract (for example, selling costs) are included in the initial measurement of the performance obligations. The Boards propose that an entity should recognize those costs as expenses unless they qualify for recognition as an asset in accordance with other standards.*

(a) Do you agree that any amounts an entity charges a customer to recover the costs of obtaining the contract should be included in the initial measurement of an entity's performance obligations? Why or why not?

(b) In what cases would recognizing contract origination costs as expenses as they are incurred not provide decision-useful information about an entity's financial position and financial performance? Please provide examples and explain why.

Response: Microsoft agrees that any amounts an entity charges a customer to recover the costs of obtaining the contract should be included in the initial measurement of the entity's performance obligation and that an entity should recognize those costs as expenses unless they qualify for recognition as an asset in accordance with other standards.

Question 12— *Do you agree that the transaction price should be allocated to the performance obligations on the basis of the entity's standalone selling prices of the goods or services underlying those performance obligations? Why or why not? If not, on what basis would you allocate the transaction price?*

Question 13— *Do you agree that if an entity does not sell a good or service separately, it should estimate the standalone selling price of that good or service for purposes of allocating the transaction price? Why or why not? When, if ever, should the use of estimates be constrained?*

Response (Questions 12 and 13): We agree that the transaction price should be allocated to the performance obligations on the basis of the entity's standalone selling prices and, if those good or service are not sold separately, an entity should estimate the standalone selling price of that good or service for purposes of allocating the transaction price. Microsoft does not believe the reasonable use of estimates should be constrained.