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Technical Director
Financial Accounting Standards Board
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DIRECTV appreciates the opportunity to comment on the Exposure Draft of proposed Accounting Standards Update (Revised), Revenue from Contracts with Customers (the "Revised ED").

DIRECTV distributes digital entertainment programming via satellite to over 30 million residential and commercial subscribers in the United States and Latin America.

We commend the Financial Accounting Standards Board (the “FASB”) and the International Accounting Standards Board (“IASB”, collectively the “Boards”) for developing a converged model for revenue recognition and agree with the Boards’ objectives described in the Revised ED. We commend the Boards for making a number of important improvements in the Revised ED, including an improved definition of a “distinct” performance obligation, a clarified definition of “transaction price”, a limit to performance obligations for renewal periods and additional services and the recording of subsequent adjustments to credit risk in the same line item as the initial estimate. We have identified a number of opportunities to improve the standard as discussed in the sections below.

In order to receive DIRECTV service, our subscribers must use a set-top receiver and other equipment. In our current business model, we retain title to most set-top receivers provided to subscribers. We sometimes collect an upfront fee in connection with the provision and installation of upgraded or additional set-top receivers to both new and existing subscribers. We have also sold the set-top receivers in the past, and could do so again in the future. As such, we have also provided comments on the Revised ED in regards to the sale of set-top receivers.

**Permit, rather than require, deferral of costs to fulfill and obtain a contract**

The final standard should permit, rather than require, the deferral of contract fulfillment costs and contract acquisition costs for entities that have a large population of homogeneous contracts. We
expense such costs because 1) deferral results in reduced transparency due to a complicated and inconsistent recognition pattern for revenues and expenses under the contract, and 2) we do not view these costs as substantially different from the costs that we would expense pursuant to Paragraph 93. If we were to defer these costs (such as installation expense and third-party commissions), we would possibly end up with a partial expense/partial deferral model for the costs to fulfill and obtain a contract because the anticipated margins over the minimum contractual commitment may be less than the amount of contractual costs we may incur for some customers. Also, Paragraph 98 indicates that the amortization period for these costs should consider renewal periods, which seems inconsistent with the impairment guidance in Paragraph 101, which requires measurement of impairment without consideration of renewals (by reference to Paragraphs 50-52 regarding the determination of the transaction price).

Based on the Revised ED, we expect to treat the revenues from contracts with our subscribers and the related costs over the typical two year contract period as follows:

Revenues

- The portion of the transaction price related to programming and the lease of set-top receivers, net of any discounts, would be recognized over the minimum contract period, which is typically two years.
- For sold set-top receivers: a portion of the transaction price would be recognized at the time of activation.

Programming and other costs of services

- Programming and other costs of services will be recognized as incurred over the two-year contract period.

Subscriber acquisition costs

- Advertising costs would be expensed immediately as a period costs.
- Costs to obtain and fulfill a contract (sales commissions and installation costs): potential for partial expense at inception for costs not deemed recoverable for some customers and partial deferral of the remaining costs over an estimated average subscriber life of at least four years, since renewal periods would be included in the amortization period pursuant to Paragraph 98.
For leased set-top receivers: Costs will be capitalized and depreciated over estimated useful life of equipment of three to seven years.

For sold set-top receivers: Costs will be expensed at the time of activation.

In addition to the complexities above, there is a potential inconsistency in accounting treatment that further supports the option to expense the costs as incurred. Applying the guidance for fulfillment costs (Paragraphs 91-93) and costs of obtaining a contract (Paragraphs 94-97) in the Revised ED could result in different accounting treatment for items that are economically the same. For example, at times we have provided discounted or free equipment to our new subscribers. If this equipment were sold directly by us (i.e. not by a third-party), costs associated with the discounted equipment would be expensed as a cost of sales at the time the equipment is activated, since the equipment is a distinct performance obligation. Conversely, if the equipment is purchased through a third-party, we may pay the third-party an increased commission which is expected to compensate them for the cost of providing the subscriber discounted or free equipment. In this situation, the increase in the commission would be considered a cost to obtain the contract, and thus would be expensed over the estimated customer life. Although both such transactions are our costs of providing discounted equipment, the mechanics of the transactions result in different accounting treatment based on the definitions in the Revised ED.

The deferred assets for costs to fulfill and obtain a contract are subject to continuous impairment analysis and periodic impairment charges that further complicates the accounting and would be impractical to efficiently apply for our over 30 million subscribers.

The practical expedient in Paragraph 97 to expense costs to obtain a contract would not be available to us because most of our contracts exceed one year, and Paragraph 98 would nonetheless require us to take into consideration anticipated renewal periods when making this determination.

In summary, deferral of costs to obtain and fulfill contracts will not provide the most relevant and understandable reporting of our operating results, and the related requirements to monitor impairment and amortization periods for each individual subscriber would be administratively impractical. Therefore, the ability to make an election to expense these costs would be a welcome improvement.
We also believe that the deferral of contract fulfillment and acquisition costs beyond the initial contract period may not be appropriate because we have no control over the asset beyond the initial contract period, and control is an essential characteristic necessary to carry an asset. The control rests with the customer, who has the ability to cancel or renew. Accordingly, any deferral period should be limited to the minimum contractual period.

Simplify the contract modification guidance

We can contemplate modifications to our contracts that may include one-time fees and contract extensions that might require us to adjust cumulative recorded revenue or prospective amortization of deferred revenue under Paragraph 22 of the Revised ED. Each of these contract modifications would be individually immaterial on our large population of homogeneous contracts. Such cumulative or prospective adjustments would be systematically impossible. We recommend that the Boards allow for a practical expedient for entities that have a large population of homogeneous contracts to treat modifications as if they are separate contracts per Paragraph 21.

Acceleration of revenue for equipment sold (similar to the Telco/handset issue)

While we currently lease most set-top receivers provided to customers, we nonetheless join with other telecommunications service providers in our concern over the aggressive allocation of revenues to deeply discounted equipment sold and delivered at the inception of a contract. We recognize the Boards have specifically debated this issue, however we would encourage the Boards to reconsider this point. The combined requirements in the Revised ED result in the potential to allocate a substantial portion of revenues from a contract to distinct performance obligations at the inception of a contract while simultaneously deferring costs to obtain and fulfill a contract well beyond the minimum contract period. We find this combined result not only complicated to apply but extremely aggressive, as it not only results in the acceleration of revenue recognition, but also provides an incentive to maximize revenues at the inception of a contract by providing more costly equipment. We believe the Boards should reconsider this topic.

One option may be to allow entities to combine such elements with other performance obligations where the asset transferred is an inseparable part of the services provided. In our case, set-top-receivers have no utility to a subscriber if they are not purchasing our service and the only way to obtain our service is with one of our set-top receivers. Accordingly, the idea that we would record a
substantial amount of revenues for the installation and transfer of title of this equipment (when sold instead of leased) seems inconsistent with the economics of the transaction, as we would never sell such equipment separately. In taking a very customer centric view of revenue recognition in the Revised ED, handsets and set-top receivers “sold” at the inception of a contract now appear to be distinct performance obligations despite the fact that many in the industry view the provision of these assets as merely a means to provide the service. This aggressive result applies not only to equipment directly related to the service, but other goods and services an entity could offer as a marketing tool. For example, the Revised ED would have us recognize revenue at inception of a contract for the delivery of a free DVD player offered as an incentive to new subscribers, despite the fact that the cost of such items is economically similar (from the reporting company’s perspective) to paying a higher sales commission.

Similarly, the definition of costs to fulfill a contract could be broadened to include assets that may otherwise be distinct, but are essential to the delivery of a service over the life of a contract. For example, we do not see a significant difference between the set-top receiver (when sold) and the dish antenna or cable we install at a subscriber’s residence. The former seems to meet the definition of a distinct performance obligation, while the latter seem to be more like “supplies used in the providing services to the customer.” We believe the Boards could develop qualitative characteristics an entity would consider in reaching this conclusion, such as whether the item is offered for free or at a deep discount or whether the entity uses early cancellation fees or similar charges to recover the cost of the equipment when a customer cancels early.

We understand others have proposed a residual approach whereby Paragraph 73(c) would be modified to apply also to assets which are sold on a standalone basis infrequently or under different circumstances. We think this is a logical alternative, as we would rarely sell set-top receivers to a non-subscriber. Likewise, subsequent sales of additional equipment to existing subscribers would represent “different circumstances” from the initial sale of equipment at the inception of a contract which would imply that those transactions should not be used to value equipment sold with new contracts to new customers.

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Again, we appreciate the opportunity to comment on the Revised ED. If you have any questions regarding our comments, please feel free to contact John Murphy at 310-964-0714 or Steve Adams at 310-964-0807.

Sincerely,

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