June 29, 2015

Susan M. Cosper, Technical Director
FASB
401 Merritt 7
PO Box 5116
Norwalk, CT 06856-5116

Via Email to director@fasb.org

Re: File reference number 2015-250

Dear Ms. Cosper:

Grant Thornton LLP appreciates the opportunity to comment on Proposed Accounting Standards Update, Revenue from Contracts with Customers (Topic 606): Identifying Performance Obligations and Licensing. We support the Board’s efforts to clarify the standard and improve the examples to assist stakeholders in applying the new revenue recognition standard.

Our answers to the questions for respondents follow. We expand on the comments in this section and offer various other points in the Appendix, including substantive comments and minor drafting points related to the proposed revisions.

Responses on Invitation to Comment questions

Question 1: Paragraphs 606-10-25-14(b) through 25-15 include guidance on accounting for a series of distinct goods and services as a single performance obligation. Should the Board change this requirement to an optional practical expedient? What would be the potential consequences of the series guidance being optional?

We believe the Board should make the series guidance optional. Making that guidance optional would reduce complexity and cost in applying the guidance, as companies would not be required to develop accounting policies, systems, and internal controls to evaluate whether goods or services meet the criteria to be recognized as a series. At the same time, companies that want to apply the series guidance to their contracts would still have the ability to do so.

Question 2: Paragraph 606-10-25-16A specifies that an entity is not required to identify goods or services promised to a customer that are immaterial in the context of a contract. Would the proposed amendment reduce the cost and complexity of applying Topic 606? If not, please explain why.

We support providing relief for entities struggling with identifying promised goods or services. However, we are not in favor of the use of the term “immaterial” as introduced in the first sentence of paragraph 606-10-25-16A. That term is generally applied at the financial statement level and introducing the need to evaluate materiality at the contract level could result in
unnecessary complexity when the Board’s intent is to simplify application. We suggest instead that the Board use the term “insignificant.” Constituents have a better understanding of the meaning of “significant” and how to apply that term. Using “insignificant” would also align with the Step 3 guidance of evaluating whether a contract contains a significant financing component.

**Question 3:** Paragraph 606-10-25-18A permits an election to account for shipping and handling as an activity to fulfill a promise to transfer a good if the shipping and handling activities are performed after a customer has obtained control of the good. Would the proposed amendment reduce the cost and complexity of applying Topic 606? If not, please explain why.

We believe that the proposed addition of ASC 606-10-25-16A makes the proposed guidance in ASC 606-10-25-18A unnecessary. We are concerned about unintended consequences that could result from characterizing shipping and handling as fulfillment activities. For example, the proposed guidance would apply to all shipping and handling (not solely to shipping and handling when the activities are determined to be insignificant), and, as a result, there could be diversity in practice: Some entities with significant shipping activities might choose to evaluate those activities as a performance obligation, and other entities with similar activities might elect to treat shipping and handling as a fulfillment activity. That could arise both when shipping is costly, such as with large, complex equipment, as well as when small consumer goods are shipped and the cost of shipping is relatively large in comparison with the goods. Instead, we believe that shipping and handling activities should be evaluated with all other promised goods or services under the guidance in ASC 606-10-25-14 through 25-22.

**Question 4:** Would the revisions to paragraph 606-10-25-21 and the related examples improve the operability of Topic 606 by better articulating the separately identifiable principle and better linking the factors to that principle? If not, what alternatives do you suggest and why?

We believe that the proposed changes to ASC 606-10-25-21 will improve the operability of ASC 606.

**Question 5:** Would the revisions to paragraphs 606-10-55-54 through 55-64, as well as the revisions and additions to the related examples, improve the operability of the implementation guidance about determining the nature of an entity’s promise in granting a license? That is, would the revisions clarify when the nature of an entity’s promise is to provide a right to access the entity’s intellectual property or to provide a right to use the entity’s intellectual property as it exists at the point in time the license is granted? If not, what alternatives do you suggest and why?

We believe that the revisions will improve the operability of the license implementation guidance in part because the guidance and related examples are very specific and appear to stipulate which types of licenses are functional and which are symbolic rather than relying on the general principles in the standard. We are concerned, however, that because the examples
illustrate narrow fact patterns addressing specific questions, entities might have difficulty applying the guidance to fact patterns that differ only slightly from the illustrative examples. In addition, business models are continually evolving and we believe that clearly defined principles, rather than narrow examples, would be easier to apply to new intellectual property and would produce more consistent results over time. For example, software business model offerings have evolved from traditional software products to include hosted arrangements, and guidance was developed in response to this evolution. We question whether stronger principles in ASC 606 would stand the test of time better than incremental illustrative guidance.

Question 6: The revisions to paragraph 606-10-55-57 that state an entity should consider the nature of its promise in granting a license of intellectual property when accounting for a single performance obligation. Does this revision clarify the scope and applicability of the licensing implementation guidance? If not, why?

We believe the proposed revisions clarify the scope and applicability of the licensing implementation guidance. However, we further believe the guidance should apply only when the license is the predominant item in the performance obligation. As drafted, it appears that this guidance would apply whenever a single performance obligation includes a license and one or more goods or services, and not solely when the license is deemed to be the predominant item in the performance obligation. We observe that the term “predominant” is introduced in proposed revisions to ASC 606-10-55-65 that solely address sales-based or usage-based royalties, and we believe that the concept of predominant should be introduced in the broader licensing guidance that includes ASC 606-10-55-57. We note that the Joint Transition Resource Group at its October 31, 2014 meeting discussed clarifying the guidance when the license is neither an insignificant nor a dominant component.

Question 7: Would the revisions to paragraph 606-10-55-64 adequately communicate the Board’s intent (a) that restrictions of time, geographical region, or use in a license of intellectual property are attributes of the license (and therefore, do not affect the nature of an entity’s promise in granting a license or its assessment of the goods or services promised in a contract with a customer) and (b) about determining when a contractual provision is a restriction of the customer’s right to use or right to access the entity’s intellectual property? If not, what alternatives do you suggest and why?

In our view, these revisions and the related example clarify the Board’s intent regarding the impact of contractual restrictions on an entity’s evaluation of an intellectual property license. We believe clarity could be enhanced by rewording and shortening the text of paragraph 606-10-55-64a as follows:

Restrictions of time, geographical region, or use—Those restrictions define the attributes of the promised license and the scope of a customer’s right to use or right to access intellectual property. Therefore, they do not define whether the entity satisfies its performance obligation at a point in time or over time or affect how many goods or services are promised in the contract. A restriction defines the scope of a customer’s right to use or right to access intellectual property. Therefore, an entity assesses whether a
contractual provision defines the scope of the customer’s right to use or right to access the intellectual property to determine whether that provision is a restriction.

We believe the final sentence in proposed paragraph 606-10-55-64a is unnecessary.

Question 8: Would paragraphs 606-10-55-65 through 55-65B and the related example clarify the scope and applicability of the guidance on sales-based and usage-based royalties promised in exchange for a license of intellectual property? If not, what alternatives do you suggest and why?

Yes.

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We would be pleased to discuss our comments with you. If you have any questions, please contact Lynne Triplett, partner, 312-602-8060, lynne.triplett@us.gt.com, or Doug Reynolds, partner, 617-848-4877, doug.reynolds@us.gt.com.

Sincerely,

/s/ Grant Thornton LLP
Appendix

**Detailed comments and suggestions**

In addition to our previous responses, we offer the following detailed comments and drafting suggestions.

**Identifying performance obligations**

ASC 606-10-25-21c: We believe it would be helpful to retain the final sentence that is marked for deletion in this paragraph.

ASC 606-10-55-140A: The final phrase “and any other supplies or services required by the customer” seems to imply that not all goods and services have been identified and that the contract is subject to further negotiation. We believe it would be difficult to determine whether yet-to-be identified goods and services are highly interrelated and highly interdependent with the goods and services in the contract. Said another way, if the goods and services have not been identified, how do you assess whether there is significant integration of those goods and services?

ASC 606-10-55-150F: The meaning of the phrase “as compared with the level of interrelation or interdependence between the equipment and the installation services in Case C” is unclear. Because the conclusion is the same in both Case C and Case D, a comparison or contrast is not evident; therefore, we suggest that this phrase be deleted.

ASC 606-10-55-309 through 55-315: It’s unclear how an entity would conclude that 20 hours of training is material in the context of the contract and then reach a conclusion that the training is separately identifiable from the product. The structure of the revision to ASC 606-10-55-309 appears to directly link helping the customer optimize its use of the product in a short time frame with the conclusion that the training is material. No explanation beyond those words is provided as to how the entity reached that conclusion (that is, no qualitative or quantitative considerations were analyzed). Accordingly, we recommend that the quantity of training hours be removed from the fact pattern or, if the example is intended to illustrate how the entity reached the conclusion of “material,” the example should be expanded to address the entity’s thought process leading to the conclusion. We are concerned about unintended consequences from this example, including diversity in practice in determining how insignificant items are treated.
Licensing
ASC 606-10-55-59a: In this discussion of functional intellectual property, the parenthetical phrase starts with “for example, the ability to process….” This structure implies that the listed items are not the only forms of functionality, yet throughout the examples that follow, this list is continually referenced as if it is the only way to conclude that intellectual property has stand-alone functionality. If that is the Board's intent, we suggest removing the phrase “for example.” An alternative resolution is to revise a fact pattern(s) in the examples to conclude that intellectual property not on that list is functional, and to explain why.

ASC 606-10-55-59b and 55-60: This discussion of symbolic intellectual property does not provide a principle that stands on its own when evaluating intellectual property. For example, in the case of an inactive sports team name and logo or a brand owned and licensed by an entity that does not use the brand in its operations, the entity has no ongoing activities, and the intellectual property therefore derives substantially all of its utility from its association with past activities (and not necessarily the activities of the entity). Functional intellectual property also derives its stand-alone functionality from past activities. Said another way, substantially all of the utility of functional intellectual property is derived from its association with past activities, either those of the entity or another entity. As such, we believe there will be confusion and potential diversity in practice in applying the guidance in that some entities might conclude that an inactive sports team name and logo is functional intellectual property and that the revenue should therefore be recognized at a point in time because, for example, the licensor never had any activities associated with that team.

ASC 606-10-55-368 through 55-370: This example concludes that the license and the manufacturing service are not distinct and are therefore a single performance obligation. With the proposed revisions to ASC 606-10-55-57, it appears the entity should determine the nature of its promise in granting the license before applying the general guidance in ASC 606-10-25-23 through 25-30. As a result, ASC 606-10-55-370 should be conformed to reflect the changes in ASC 606-10-55-57.

ASC 606-10-55-377: It is unclear whether the added phrase “and is available from sources other than the entity” is required for the analysis of identifying performance obligations, or, if it is required, how. We believe that the license qualifies for “distinct” because it can be used with other readily available resources, such as the equipment delivered before the opening of the franchise in this fact pattern.

Examples 58 and 59: We believe these examples illustrate how difficult it will be to apply the concept of stand-alone functionality to various types of licenses and obtain consistent outcomes. In Example 58 (paragraph 606-10-55-386), a conclusion is reached that character names and images do not have stand-alone functionality separate from “significant additional production…” However, in Example 59 (paragraph 606-10-55-391), a conclusion is reached that the symphony recording has stand-alone functionality because “the recording can be played in its present, completed form.” One could argue that there is no distinction between the characters (which might no longer be in production but may be usable in their current form) and the symphony recording (which is usable in its current form). In the example of the...
Examples
In general, we believe the revised and new examples in the proposed ASU include illustrations of fact patterns that are too narrow and provide too much detail. We are concerned about potential unintended consequences resulting from this level of detail.

For example, the penultimate sentence in ASC 606-10-55-399 indicates that the entity should evaluate whether it can apply the practical expedient in ASC 606-10-55-18 to recognize amounts as they are billed, despite the guidance in ASC 606-10-55-65, which states that revenue for a sales-based royalty promised in exchange for a license of intellectual property is recognized only when the subsequent sale occurs. We believe this unnecessarily increases the complexity in applying the guidance to contracts that include a license of intellectual property with payment in the form of sales-based and usage-based royalty. We also believe that the meaning of the last sentence in ASC 606-10-55-399 is unclear. The final phrase indicates that the entity has concluded that periodic recognition of both the fixed amount and the sales-based royalty is an appropriate measure of progress; however, no measure of progress is included in the example. We suggest that the two final sentences of ASC 606-10-55-399 be deleted to increase the clarity of the example.

In addition, we believe that in the example in ASC 606-10-55-377, the added phrase “and is available from sources other than the entity” seems unnecessary and might cause constituents to conclude when evaluating the criteria in ASC 606-10-25-19 that a good or service must be available from other sources to be distinct. Also, in ASC 606-10-55-393, it is unclear whether the fact that the customer is able to display the memorabilia “before” the six-week airing period is significant. If not, we suggest deleting the word “before” from the example to avoid unintended consequences.

Minor drafting comments
ASC 606-10-55-140A: If the final sentence is retained as is, we suggest deleting “any.”

ASC 606-10-55-143: Delete “Therefore” at the beginning of the third sentence.

ASC 606-10-55-150A: Rephrase the final sentence to read as “The installation required can be performed by several alternative service providers.” We believe it is inappropriate to describe installation as being “capable.” The point appears to be that the installation is readily available from other vendors.

ASC 606-10-55-153: The final sentence is inconsistent with the other examples of identifying performance obligations because the other examples do not end with a statement about allocation. We suggest adding the same text to each of the other examples illustrating the Step 2 guidance to make them all consistent.
ASC 606-10-55-388: The second sentence duplicates the guidance in the first sentence because ASC 606-10-55-58A includes a statement that preparers should look to ASC 606-10-25-31 through 25-37 to select an appropriate method to measure progress.

ASC 606-10-55-399E: Revise the wording in the second sentence to say “…assuming the content is made available on or before that date.”