

Revenue — FASB Decides to Issue ASU on Performance Obligations and Licenses

October 8, 2015 — The FASB met on October 5, 2015, to redeliberate — on the basis of the comment letters it received — its [proposal](#)¹ to amend the guidance in [ASU 2014-09](#)² on (1) identifying performance obligations and (2) licenses. (See Deloitte's May 13, 2015, [Heads Up](#) for more information about the proposed ASU.) The Board reaffirmed most of the proposed amendments at this meeting.³

Topics discussed in connection with identifying performance obligations included:

- The principle for evaluating whether a promise constitutes a separately identifiable performance obligation.
- Goods or services that are immaterial in the context of a contract.
- A practical expedient allowing an entity to account for shipping and handling as fulfillment costs.
- Cost accruals when a promise is immaterial in the context of the contract or when the entity applies the practical expedient for shipping and handling costs.
- Whether it should be optional to apply the series guidance in ASC 606-10-25-15.⁴
- The scope of the practical expedient in ASC 606-10-50-14 with respect to disclosures about remaining performance obligations.

Topics discussed in connection with licenses included:

- Determining the nature of an entity's promise in granting a license when the license is not a separate performance obligation.
- The scope of the sales- or usage-based royalty constraint.
- Restrictions on the use of a license.

¹ FASB Proposed Accounting Standards Update, *Identifying Performance Obligations and Licensing*.

² FASB Accounting Standards Update No. 2014-09, *Revenue From Contracts With Customers*.

³ For more information about the topics discussed at the meeting, including a summary of the comment-letter feedback received, see the FASB's October 5, 2015, meeting [handout](#).

⁴ For titles of *FASB Accounting Standards Codification* (ASC) references, see Deloitte's ["Titles of Topics and Subtopics in the FASB Accounting Standards Codification."](#)

Identifying Performance Obligations

The Board reaffirmed the following proposed amendments:

- *Separately identifiable principle* — The proposed ASU would clarify the separately identifiable principle by (1) providing “three factors that indicate that an entity’s promises to transfer goods or services to a customer are not separately identifiable” in a manner consistent with the notion of separable risks and (2) indicating when a good or service would not be separable in the context of the contract.
- *Immaterial promised goods or services* — Entities would be permitted to disregard goods or services promised to a customer that are immaterial in the context of the contract.
- *Shipping and handling activities* — A practical expedient to allow shipping or handling activities occurring after control has passed to the customer to be treated as a fulfillment cost rather than as a revenue element (i.e., a promised service in the contract).

The Board also agreed that cost accruals would be required when an entity deems a promise to be immaterial in the context of a contract or when the entity applies the practical expedient related to shipping and handling.

Editor’s Note: Two Board members have indicated that they disagree with issuing a final ASU based on the proposal. Part of the reason for their dissent is the proposed guidance on immaterial goods or services. Their specific concerns include:

- They do not think that the word “material” should be used.
- Clarifying immaterial items will only create more confusion.
- It is not necessary to explain what entities did not have to assess.
- Highlighting immaterial items would not be important to financial statement users.

Further, the Board discussed whether the series provision in ASC 606-10-25-14(b) through 25-15 should continue to be required when the criteria are met or whether it should be optional. The Board decided not to make this guidance optional.

The Board also decided not to expand the scope of the disclosure practical expedient for remaining performance obligations in ASC 606-10-50-14. Some Board members indicated that there has been limited feedback from preparers, and no feedback from financial statement users, on this topic.

However, the Board directed the staff to further research situations in which entities accumulate information to comply with the transaction price disclosure requirements in ASC 606-10-50-13 but do not use such information for recognition and measurement under the new revenue model. This research will be separate from the project on identifying performance obligations and licensing.

Licenses

The Board reaffirmed the proposed amendments on:

- *Determining the nature of an entity's promise in granting a license* — The proposed amendments to the implementation guidance would require entities to determine whether the license grants customers a right to use the underlying intellectual property (IP) (which would result in point-in-time revenue recognition) or a right to access the IP (which would result in revenue recognition over time).
- *The distinction between two types of licenses: (1) functional IP and (2) symbolic IP* — Functional IP would represent a right to use the IP and would be recognized at a point in time (unless there is a requirement to update the IP and this requirement is not a separate performance obligation, in which case it would be accounted for as a right to access and would be recognized over time), whereas symbolic IP would represent a right to access and would be recognized over time.
- *The nature of an entity's promise in granting a license* — An entity would be required to consider the nature of this promise when accounting for a single performance obligation that includes the license of IP and one or more goods or services in instances in which the license is not distinct and not a separate performance obligation.

The Board rejected including an “override” to the proposed guidance on symbolic IP. As described in the Board meeting handout, this proposal would have allowed for point-in-time revenue recognition “if the contract does not require, and the customer does not expect, the entity to support or maintain the [IP] during the license period” for symbolic licenses.

Royalties

The Board reaffirmed that:

- A royalty should not be bifurcated into a portion accounted for in accordance with the sales- and usage-based royalty constraint and a portion accounted for in accordance with the general guidance on variable consideration.
- The sales- and usage-based royalty constraint would be applicable when the predominant item related to the royalty is a license of IP.

In addition, the FASB affirmed that, as described in the Board meeting handout, “an entity recognizes revenue from a sales-based or usage-based royalty when a customer's subsequent sales or usage occur unless recognition in that manner would accelerate the recognition of revenue for the performance obligation to which the royalty relates ahead of the entity's performance toward complete satisfaction of the performance obligation.”

The Board voted against:

- Expanding the scope of the royalty constraint to include sales of IP as well as licenses of IP.
- Amending ASC 606 to address the issue of in-substance sales of IP.

Restrictions

The Board also reaffirmed that restrictions in a license are attributes of the license and therefore do not alter the number of licenses in the contract. The Board discussed that an entity should evaluate the terms and conditions of a contract to determine the attributes of a license (e.g., restrictions of time, geography) and the promises to the customer in the contract. The FASB staff explained that entities must use judgment in making this determination.

Editor's Note: Two Board members expressed their view that the proposed illustrative examples related to restrictions were not clear. Contractual restrictions will be discussed at the November 9, 2015, meeting of the FASB-IASB joint transition resource group (TRG) for revenue recognition. The FASB staff will consider the feedback from that meeting. If the staff determines that major changes are needed after evaluating that feedback, the Board may decide to incorporate the clarifications related to contractual restrictions into a separate ASU.

Next Steps

The Board has directed the staff to begin drafting a final ASU on identifying performance obligations and licenses.

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