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July 23, 2019

TO: MEMBERS OF THE FASB EMERGING ISSUES TASK FORCE

Included are the final minutes of the June 13, 2019 meeting of the FASB Emerging Issues Task Force (EITF).

On June 26, 2019, the Board ratified the Task Force consensus-for-exposure on Issue 19-A (Interactions between Topic 321, Topic 323, and Topic 815). The proposed Update for Issue 19-A is expected to be posted to the FASB website in late July with a comment letter deadline in late August.

The next regular EITF meeting is scheduled for September 19, 2019.

Please call or email me if you have any questions.

Sincerely,

Jason Bond

FASB Practice Fellow



Financial Accounting Standards Board

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**Emerging Issues Task Force
Meeting Minutes
June 13, 2019**

	<u>Pages</u>
• Attendees	1
• Administrative Matters	2
• Discussion of Agenda Technical Issues	3-22
1. Issue No. 18-A, “Recognition under Topic 805 for an Assumed Liability in a Revenue Contract”	3-12
2. Issue No. 19-A, “Financial Instruments—Clarifying the Interactions between Topic 321, Topic 323, and Topic 815”	13-18
3. Issue No. 19-B, “Revenue Recognition—Contract Modifications of Licenses of Intellectual Property”	19-22

**MINUTES OF THE JUNE 13, 2019 MEETING
OF THE FASB EMERGING ISSUES TASK FORCE**

Location: FASB Offices
401 Merritt 7
Norwalk, Connecticut

Thursday, June 13, 2019

Starting Time: 8:30 a.m.

Concluding Time: 12:30 p.m.

Task Force Members Present:

Susan M. Cosper, FASB Board Member (EITF Chairman)

Kimber K. Bascom

Paul Beswick

James G. Campbell

Terri Z. Campbell (by telephone)

Lawrence N. Dodyk

Bret Dooley

Ashwinpaul C. (Tony) Sondhi (by telephone)

Robert Uhl

Eric West

Liesl Nebel (incoming member)

Matthew Schechter (incoming member)(by telephone)

Angela J. Newell (FinREC Observer)

Kevin Vaughn (SEC Observer)

*Yan Zhang (PCC Observer)(by telephone)

Others at Meeting Table:

Russell G. Golden, FASB Chairman

Christine A. Botosan, FASB Board Member

Gary R. Buesser, FASB Board Member

Marsha L. Hunt, FASB Board Member

R. Harold Schroeder, FASB Board Member

Shayne B. Kuhaneck, Acting FASB Technical Director

Jason C. Bond, FASB Practice Fellow

*Ryan J. Carter, FASB Project Manager

*Christopher Cryderman, FASB Practice Fellow

*Mary S. Mazzella, FASB Senior Project Manager

*Bobbi S. Gwinn, FASB Assistant Project Manager

Jane M. Lazzara, FASB Postgraduate Technical Assistant

Tyler M. Padgett, FASB Postgraduate Technical Assistant

*Douglas A. Jepsen, FASB Postgraduate Technical Assistant

* For certain Issues only.

ADMINISTRATIVE MATTERS

- The EITF Coordinator noted that there are now three active Issues on the EITF agenda.
- The EITF Coordinator announced that any consensus or consensus-for-exposure reached at this meeting would be considered by the Board for ratification at the June 26, 2019 Board meeting.
- The EITF Chair announced that Mr. Mark LaMonte and Mr. Alex Corl have stepped down as members of the Task Force effective as of the January 21, 2019 EITF meeting. The Chair thanked Messrs. LaMonte and Corl for their service.
- The EITF Chair announced that Mr. Tony Sondhi, A.C. Sondhi & Associates, LLC, has completed his service as a member of the Task Force effective with the June 13, 2019 EITF meeting. The Chair thanked Mr. Sondhi for his service.
- The EITF Chair announced that Mr. Jim Dolinar, Crowe LLP, has completed his service as the EITF Observer representing FinREC effective as of the January 21, 2019 EITF meeting and welcomed Ms. Angela Newell, BDO USA, LLP, as the new EITF Observer representing FinREC effective as of the June 13, 2019 EITF meeting. The Chair thanked Mr. Dolinar for his service.
- The EITF Chair welcomed Mr. Jeremy Perler, Schilit Forensics; Ms. Liesl Nebel, Schoolhouse; and Mr. Matthew Schechter, formerly of Balyasny Asset Management, as the newest members of the Task Force.
- The EITF Coordinator announced that the next regular EITF meeting is scheduled for September 19, 2019, and that the “Extra” EITF meeting reserved for July 11, 2019, would not be utilized.
- The EITF Coordinator announced that the 2020 EITF meeting dates have been confirmed and will be posted to the FASB website. Those dates are:

2020 REGULAR MEETING DATES

March 12, 2020
June 11, 2020
September 3, 2020
November 5, 2020

2020 EXTRA MEETING DATES

January 23, 2020
May 21, 2020
July 30, 2020
October 8, 2020

DISCUSSION OF AGENDA TECHNICAL ISSUES

Issue No. 18-A

Title: Recognition under Topic 805 for an Assumed Liability in a Revenue Contract

Dates Discussed: June 7, 2018; September 27, 2018; June 13, 2019

Background

1. Topic 805 provides guidance on the accounting for business combinations. In applying the acquisition method in Topic 805, an acquirer recognizes identifiable assets acquired and liabilities assumed in a business combination and generally measures those assets and liabilities at fair value. Paragraph 805-20-25-2 provides further guidance on the recognition criteria. It states that for an identifiable asset or liability assumed to be recognized in a business combination, it must meet the definition of an asset or liability in FASB Concepts Statement No. 6, *Elements of Financial Statements*. Concepts Statement 6 defines liabilities as “probable future sacrifices of economic benefits arising from present obligations of a particular entity to transfer assets or provide services to other entities in the future as a result of past transactions or events.” The definition in Concepts Statement 6 also clarifies that a present obligation is broader than a legal obligation.
2. EITF Issue No. 01-3, “Accounting in a Business Combination for Deferred Revenue of an Acquiree,” provided specific guidance on the accounting for deferred revenue in a business combination. Issue 01-3 required an acquiring entity to recognize a liability related to the deferred revenue of an acquired entity only if that deferred revenue represented a legal obligation assumed by the acquiring entity (a legal performance obligation as described in Issue 01-3) and the amount assigned to that liability was its acquisition date fair value. Issue 01-3 was superseded by FASB Statement No. 141 (revised 2007), *Business Combinations*, which did not include specific guidance on the recognition of deferred revenue as a liability assumed in a business combination. Rather, Statement 141(R) referenced the definition of a liability in Concepts Statement 6 (that guidance is now codified in paragraph 805-20-25-2).
3. Although Statement 141(R) superseded the guidance in Issue 01-3, stakeholders indicated that practice generally continued to apply the concepts in Issue 01-3, including use of the legal obligation concept, to determine whether an entity should recognize a liability assumed related to deferred revenue of an acquired entity accounted for under Topic 605, Revenue Recognition.
4. In May 2014, the FASB issued Accounting Standards Update No. 2014-09, *Revenue from Contracts with Customers (Topic 606)*, which provides a single comprehensive accounting model on revenue recognition for contracts with customers. Among other things, Topic 606 defines a performance obligation as “a promise in a contract with a customer to transfer to the customer either: (a) a good or service (or a bundle of goods or services) that is distinct or (b) a series of distinct goods or services that are substantially the same and that have the same pattern of transfer to the customer.” Distinct goods or services may not be explicitly stated in the contract and can include goods or services that are implied by an entity’s customary business practices, which do not need to be legally enforceable.

5. Stakeholders have indicated that after Topic 606 is adopted, there is diversity in views on how an acquirer would evaluate revenue contracts with customers in a business combination. Some stakeholders believe that an entity should use the Topic 606 performance obligation definition to determine whether a liability in a revenue contract is a liability assumed that is recognized in the business combination, and other stakeholders believe that an entity should continue to use the legal obligation concept when applying the guidance in Topic 805.

6. On March 28, 2018, the Board added a narrow scope Issue to the EITF agenda to reduce the diversity that might arise when evaluating whether to recognize a liability from a revenue contract with a customer that is acquired in a business combination after an entity has adopted Topic 606. In addition, stakeholders have indicated that questions may arise under Topic 606 about measurement of revenue contracts with customers in a business combination. The Board asked the Task Force also to consider those measurement issues.

Issues

7. The following issues were included in Issue Summary No. 1, dated May 24, 2018, and were discussed at the June 7, 2018 EITF meeting:

- Issue 1: Recognition for an Assumed Liability in a Revenue Contract
- Issue 2: Measurement for an Assumed Liability in a Revenue Contract in a Business Combination.

8. The following issues were included in Issue Summary No. 1, Supplement No. 1, dated September 13, 2018, and were discussed at the September 27, 2018 meeting:

- Issue 1A: Payment Terms and Their Effect on Subsequent Revenue Recognition
- Issue 3: Costs to Fulfill a Performance Obligation in Measuring the Fair Value of a Contract Liability for a Revenue Contract under Topic 805.

9. At the September 27, 2018 meeting, the Task Force also discussed the previous consensus-for-exposure on Issues 1 and 2 reached at the June 2018 meeting.

10. The following issues were included in Issue Summary No. 1, Supplement No. 2, dated May 30, 2019:

- Issue 1: Recognition of an Assumed Liability from a Revenue Contract
- Issue 2: Scope
- Issue 3: Disclosures
- Issue 4: Transition and Effective Date.

11. The following issues were included in Issue Summary No. 1, Supplement No. 3, dated May 30, 2019:

- Chapter 1— Payment Terms and Their Effect on Subsequent Revenue Recognized
- Chapter 2— Costs to Fulfill a Performance Obligation in Measuring the Fair Value of a Contract Liability for a Revenue Contract under Topic 805.

12. Issues 1 through 4, and Chapters 1 and 2 were discussed at the June 13, 2019 meeting.

Prior EITF Discussion

Issue 1: Recognition for an Assumed Liability in a Revenue Contract

13. At the June 7, 2018 EITF meeting, the Task Force reached a consensus-for-exposure that would require an entity to use the Topic 606 performance obligation definition to determine whether an assumed contract liability from a revenue contract with a customer represents a liability assumed that is recognized in a business combination at the acquisition date. An entity would evaluate whether it has a liability for a revenue contract that is assumed in a business combination because the acquiree has a contract liability (that is, it has been paid for goods or services that have not been transferred to the customer). The acquirer would not recognize a liability for goods or services that have not been transferred to the customer and for which no payment has been received, except in cases in which the acquiree has recognized a receivable.

14. In reaching this consensus-for-exposure, the Task Force considered both the Topic 606 performance obligation concept and the superseded legal obligation concept as potential alternatives. The Task Force discussed the use of the legal obligation concept alternative in current practice before the adoption of Topic 606 and observed that Topic 606 did not consequentially amend Topic 805, which requires that a liability recognized in a business combination meet the definition of a liability in Concepts Statement 6. The Task Force rejected that alternative because it believes that the use of the definition of performance obligation better aligns with current guidance already included in the Codification and would be consistent between both Topic 606 and Topic 805 (that is, for the identification of an obligation for a revenue contract). In addition, the Task Force also observed that the Topic 606 performance obligation concept may be less complex to apply and is more consistent with the definition of a liability in Concepts Statement 6.

15. The Task Force indicated that in most situations the recognition conclusion under either a Topic 606 performance obligation alternative or a legal obligation alternative would be the same, but the Task Force acknowledged that there may be circumstances under which the recognition conclusion could be different, such as for symbolic licenses or goods or services that are provided as a customary business practice because the entity is not legally obligated to perform in those situations. For situations in which the Topic 606 performance obligation does not represent a legal obligation, the Task Force noted that in many cases the fair value measurement of the performance obligation may be minimal or zero because of the nature of the activity or activities that the acquirer would be performing. See the discussion on measurement considerations in Issue 2.

16. The Task Force also considered whether the timing of the payment of consideration or payment terms should affect the amount of revenue recognized by the acquirer related to the acquired revenue contract. As a part of its consensus-for-exposure, the Task Force decided that the payment terms of an acquired revenue contract should not affect the amount of subsequent revenue recognized by an acquirer after a business combination.

17. At its June 27, 2018 Board meeting, the Board ratified the consensus-for-exposure reached by the Task Force on this Issue and directed the FASB staff to draft a proposed Update reflecting the consensus-for-exposure for vote by written ballot. However, while reviewing a draft of the proposed Update, Task Force members identified potential unintended consequences of their decision on payment terms reached at the June 7, 2018 meeting. As a result, individual Task Force members recommended that the Issue be further discussed by the Task Force prior to the issuance of the proposed Update.

18. At the September 27, 2018 EITF meeting, the Task Force reached a consensus-for-exposure that would require an entity to use the Topic 606 performance obligation definition to determine whether to recognize a contract liability from a revenue contract with a customer that is acquired in a business combination at the acquisition date. An entity would evaluate whether it has a contract liability from a revenue contract that is assumed in a business combination because the acquiree has been paid (or consideration is due) for goods or services for which control has not been transferred to the customer. The acquirer would not need to perform this evaluation if the acquiree has not received payment or there is no consideration due (that is, a contract liability would not have been recognized under Topic 606). The basis for this consensus-for-exposure is the same as described in paragraphs 14 and 15.

Issue 2: Measurement for an Assumed Liability in a Revenue Contract in a Business Combination

19. In addition to the recognition issue, stakeholders indicated that questions may arise after the adoption of Topic 606 about how to determine the fair value of a contract liability when applying the acquisition method. As a result, at its March 28, 2018 meeting, the Board directed the Task Force to consider the following measurement issues to provide educational information to stakeholders:

- a. May the acquirer determine the fair value of a contract liability recognized in the business combination using the amount as determined by the acquiree in its revenue accounting (that is, a carryover basis)?
- b. Should the acquirer consider the other assets and liabilities in the acquired set when determining the value of a contract liability acquired in a business combination?

20. At the June 7, 2018 EITF meeting, the Task Force reached a consensus-for-exposure on the first measurement question that it would be inappropriate for an acquirer to default to using a carryover basis (that is, recording the liability on the acquirer's balance sheet equal to the amount of deferred revenue on the acquiree's balance sheet immediately preceding the business combination date) when measuring an assumed liability in a revenue contract because that would be inconsistent with the measurement guidance in Topic 805. The measurement principle in paragraph 805-20-30-1 states that an acquirer must measure the identifiable assets acquired, the liabilities assumed, and any noncontrolling interest in the acquiree at their acquisition-date fair values. That principle exists for all assets and liabilities acquired in a business combination under Topic 805, with some exceptions that are specified in that Topic. The Task Force noted that an exception to the fair value measurement principle in Topic 805 is not necessary for an assumed liability in a revenue contract acquired in a business combination.

21. In determining the fair value of a contract liability acquired in a business combination, the Task Force noted that the acquirer would measure the fair value of the remaining or unfulfilled performance obligation, as defined under Topic 606, that it has assumed from the acquiree. In determining the fair value of the unfulfilled performance obligation, the acquirer would consider only activities the acquirer will perform after the business combination that directly relate to the acquired contract. That is, it would not consider the overall activities the acquirer would undertake irrespective of the acquired contract or activities already performed by the acquiree that the acquirer would not perform.

22. The second measurement question focuses on what should be included in the fair value measurement and not how an entity would determine fair value. The Task Force noted that how to measure those costs is covered in the guidance in Topic 820, Fair Value Measurement, and is outside the scope of this Issue.

23. The Task Force considered two potential alternatives to determine the fair value of an assumed contract liability:

- a. *Consider the assets and liabilities in the acquired set.* This alternative would consider assets included in the acquired set when measuring the fair value of a contract liability recognized in a business combination. For example, if a contract liability is recognized in a business combination for an in-process license arrangement, the measurement of that contract liability would not assume that the acquirer would have to obtain the related intellectual property in order to perform under the acquired contract because that intellectual property was included in the acquired set. This would result in a “net” valuation of the liability as opposed to including an amount for the value of the intellectual property in both the asset and liability.
- b. *Do not consider the other assets and liabilities in the acquired set.* This alternative would consider the contract liability in isolation from any related asset needed to satisfy the performance obligation in the acquired contract even if the asset was included in the acquired set. For example, if a contract liability is recognized in a business combination for an in-process license arrangement, the measurement of that contract liability would assume that the acquirer would have to obtain the underlying intellectual property in order to perform under the acquired contract. This would result in gross measurements of the asset and the liability on the balance sheet.

24. At the June 7, 2018 EITF meeting, the Task Force reached a consensus-for-exposure that an acquirer would consider the assets and liabilities in the acquired set when determining the fair value of an assumed contract liability because ignoring an asset in the acquired set that is necessary to fulfill the liability would not be appropriate when the asset and liability have been acquired and assumed, respectively, together. The Task Force indicated that a buyer generally would not assume an obligation in a business combination to perform under a contract without also purchasing the asset needed to fulfill that contract. Therefore, the Task Force noted that it would be appropriate to value that obligation after considering the related asset. In reaching this consensus-for-exposure, the Task Force indicated that it would not want to allow an acquirer to recognize higher revenue after a business combination because of a valuation technique used to measure a contract liability.

25. At its June 27, 2018 Board meeting, the Board ratified the consensus-for-exposure reached by the Task Force on this Issue and directed the FASB staff to draft a proposed Update reflecting the consensus-for-exposure for vote by written ballot. However, while reviewing a draft of the proposed Update, Task Force members identified potential unintended consequences of the decisions reached at the June 7, 2018 meeting. As a result, individual Task Force members recommended that the Issue be further discussed by the Task Force prior to the issuance of the proposed Update.

Invitation to Comment—Measurement and Other Considerations Related to Revenue Contracts with Customers under Topic 805

26. At the September 27, 2018 EITF meeting, the Task Force considered the measurement of the assumed contract liability (Issues 2 and 3) and the effects of payment terms on the subsequent revenue recognition of the acquired revenue contract (Issue 1A). The Task Force decided not to address those issues at that time. The Task Force recommended to the Board that the staff issue an Invitation to Comment (separate from the proposed Update) to solicit input about measurement and other topics discussed by Task Force members.

Effective Date, Transition, and Transition Disclosures

27. At the June 7, 2018 EITF meeting, the Task Force did not propose an effective date for any proposed amendments resulting from this Issue. Consequently, the Task Force will take into consideration the comments received on any proposed amendments before determining when those amendments would be effective.

28. At the June 7, 2018 EITF meeting, the Task Force reached a consensus-for-exposure that would require that an entity apply the proposed amendments prospectively to all business combinations that occur after the proposed amendments are effective. The Task Force indicated that allowing a choice between prospective transition or modified retrospective transition would result in unnecessary costs and added complexity for preparers particularly because the Task Force noted that the financial reporting outcome resulting from the proposed amendments should not be materially different from current practice. In reaching this consensus-for-exposure, the Task Force also considered previous amendments to Topic 805, which generally followed a prospective transition method.

29. At the June 7, 2018 EITF meeting, the Task Force also reached a consensus-for-exposure not to require any transition disclosures in the period of adoption because the Task Force believes that the disclosures would not provide incremental information that would be useful to users of financial statements and therefore would result in unnecessary costs for preparers.

30. At its June 27, 2018 Board meeting, the Board ratified the consensus-for-exposure reached by the Task Force on this Issue and directed the FASB staff to draft a proposed Update reflecting the consensus-for-exposure for vote by written ballot. However, while reviewing a draft of the proposed Update, Task Force members identified potential unintended consequences of the decisions reached at the June 7, 2018 meeting. As a result, individual Task Force members

recommended that the Issue be further discussed by the Task Force prior to the issuance of the proposed Update.

31. At the September 27, 2018 EITF meeting, the Task Force did not propose an effective date for the amendments resulting from this Issue. Consequently, the Task Force will take into consideration the comments received on the proposed amendments before determining when those amendments would be effective.

32. At the September 27, 2018 EITF meeting, the Task Force reached a consensus-for-exposure that would require that an entity apply the amendments resulting from this Issue prospectively to all business combinations that occur after those amendments are effective. In reaching this consensus-for-exposure, the Task Force considered previous amendments to Topic 805, which generally followed a prospective transition method. The Task Force also indicated that allowing a choice between prospective transition or modified retrospective transition could result in unnecessary costs and complexity for preparers (for example, restating the subsequent accounting for the assets and liabilities recognized in the business combination), particularly because the Task Force noted that the financial reporting outcome resulting from the amendments resulting from this Issue may not be materially different from current practice.

33. At the September 27, 2018 meeting, the Task Force also reached a consensus-for-exposure not to require any disclosures in the period of adoption because the Task Force believes that the disclosures would not provide incremental information that would be useful to users of financial statements and therefore would result in unnecessary costs for preparers.

Board Ratification

34. At its October 10, 2018 meeting, the Board ratified the consensus-for-exposure reached by the Task Force on this Issue and directed the FASB staff to draft a proposed Update reflecting the consensus-for-exposure for vote by written ballot. In addition to the consensus-for-exposure being ratified by the Board, the FASB chairman authorized the staff to prepare a Discussion Paper in the form of an Invitation to Comment (separate from the proposed Update) to solicit input about measurement and other topics related to the Task Force's consensus-for exposure.

35. On February 14, 2019, the FASB issued proposed Accounting Standards Update, *Business Combinations (Topic 805): Revenue from Contracts with Customers—Recognizing an Assumed Liability*. The proposed Accounting Standards Update was issued concurrently with a FASB Invitation to Comment, *Measurement and Other Topics Related to Revenue Contracts with Customers under Topic 805*. The comment deadline for both documents was April 30, 2019.

Current EITF Discussion

36. At the June 13, 2019 EITF meeting, the Task Force discussed the comment letter feedback on the proposed Update and on the related Invitation to Comment (ITC). The proposed Update included a question about the implications, if any, of finalizing the proposed amendments on the recognition of a contract liability from a revenue contract with a customer acquired in a business combination without finalizing amendments on measurement and other topics that may result from feedback received as part of the concurrently issued ITC. The Task Force discussed the comment letter feedback on the ITC in advance of its vote on whether to finalize the proposed amendments.

Chapter 1—Payment Terms and Their Effect on Subsequent Revenue Recognized

37. The Task Force discussed the approach illustrated in the ITC (that is, the recognition of an identifiable asset) and the additional approaches suggested by comment letter respondents (the exception approach and net fair value approach) to achieve the objective that payment terms should not affect the subsequent amount of revenue recognized by an acquirer after a business combination. One Task Force member noted that the variety of approaches suggested by stakeholders indicates that the issue is challenging and may be better addressed holistically by the Board. Another Task Force member indicated that all of the suggested approaches have merit; however, the Board may need to evaluate the tradeoff between a practical and conceptually pure solution.

38. Two Task Force members noted that if the approach illustrated in the ITC is pursued, they would struggle conceptually with the recognition of an identifiable asset that would be required to achieve the objective that payment terms should not affect the subsequent amount of revenue recognized by an acquirer after a business combination because it is not clear what that asset would represent.

39. Several Task Force members raised concerns about the exception approach. Those Task Force members noted that allowing an exception to the general guidance in Topic 805 for revenue contracts would raise questions about other circumstances under which an exception could be provided. In addition, one Task Force member noted that the implications of requiring an exception approach would need to be further researched, as it may have different implications for entities with different types of contracts. One Task Force member also indicated that an exception approach would result in a deviation from international standards. A few Task Force members expressed support for the net fair value approach or a fair value-based approach. One Task Force member who is a preparer indicated that they do not believe such an approach would be overly complex, particularly if a portfolio approach that groups contracts with similar payment terms is permitted. Another Task Force member who is a user noted that they have concerns about users misinterpreting fair value adjustments; however, they prefer a fair-value based approach to the other approaches suggested.

40. Task Force members generally agreed that the approaches suggested to achieve the payment terms objective should be further researched to understand the implications of the various approaches. One Task Force member suggested that the staff conduct outreach with users and valuation professionals to better understand the merits of each approach. Another Task Force member noted that the Board's decision on an approach should be determined based on what is valuable to users.

Chapter 2—Costs to Fulfill a Performance Obligation in Measuring the Fair Value of a Contract Liability for a Revenue Contract under Topic 805

41. The Task Force discussed the circumstances under which an entity should include a contributory charge for the use of a related asset in measuring the fair value of a contract liability acquired in a business combination. One Task Force member indicated that a contributory charge

generally should be included in the valuation of an asset and that there should be no difference between a tangible asset and an intangible asset. Two Task Force members noted that determining an appropriate contributory charge is not complex for many types of contracts. However, both of those Task Force members noted that determining the value of a contract liability that requires the use of a unique asset to fulfill an obligation would be challenging. One of those Task Force members noted that this issue is most pronounced for licensing and royalty arrangements.

42. One Task Force member noted that it is important to apply a method that is consistent with estimated cash flows that are included in the valuation model at the time of acquisition. That Task Force member specifically noted that it would be inappropriate for an entity to recognize revenue after a business combination for a license in which the intellectual property was provided before the business combination. That Task Force member also suggested that the staff focus on how a user would develop an expectation about future revenue when further developing alternatives related to measurement.

43. One Task Force member indicated that the performance obligation unit of account used in Topic 606 should be the unit of valuation in a business combination under Topic 805.

Issue 1: Recognition of an Assumed Liability from a Revenue Contract

44. The Task Force decided not to affirm its consensus-for-exposure at this time and to wait and see what the Board decides about the measurement of contract liabilities and other issues described in the ITC. The Task Force continued to support the use of the performance obligation definition as the recognition criteria for a revenue contract with a customer acquired in a business combination. However, the Task Force indicated that the appropriate path forward would be to address the issues in the proposed Update and ITC holistically. One Task Force member noted that if the proposed amendments were finalized, the population of liabilities that would be recognized in a business combination would increase. Therefore, diversity in practice would increase by finalizing the consensus without additional measurement guidance. Another Task Force member indicated that requiring entities to undergo two transitions for interrelated issues would be burdensome.

45. Although a consensus was not reached on Issue 1, Task Force members proceeded to provide their views to the Board on Issues 2 and 3.

Issue 2: Scope

46. One Task Force member noted that contracts in the scope of Subtopic 610-20, Other Income—Gains and Losses from the Derecognition of Nonfinancial Assets, and contracts that are accounted for under other topics that apply the principles of Topic 606 should be included in the scope of the amendments resulting from this Issue. Another Task Force member indicated that the scope of any amendments resulting from this Issue should be clear rather than left to the interpretation of stakeholders.

Issue 3: Disclosures

47. Two Task Force members indicated that incremental disclosures should be considered, once recognition and measurement conclusions are reached, to facilitate a user's understanding of how the contract liability for a performance obligation assumed a business combination would subsequently affect the amount of revenue recognized by the acquirer.

Status

48. The FASB Chairman asked whether the Task Force had feedback for the Board about accounting for business combinations generally. The FASB Chairman noted that there are multiple projects on the FASB's technical agenda that relate to business combinations and solicited Task Force recommendations about how feedback on those projects should be considered moving forward.

49. The Board will consider the comment letter feedback and Task Force discussion at a future Board meeting to determine an appropriate path forward for this Issue and the related Board research project on measurement and other topics related to revenue contracts with customers under Topic 805.

Issue No. 19-A

Title: Financial Instruments—Clarifying the Interactions between Topic 321, Topic 323, and Topic 815

Date Discussed: June 13, 2019

Background

1. The FASB issued Accounting Standards Update No. 2016-01, *Financial Instruments—Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities*, in January 2016. The amendments in that Update retained the current framework for accounting for financial instruments in GAAP but made targeted improvements to address certain aspects of recognition, measurement, presentation, and disclosure of financial instruments. Equity investments that do not result in the consolidation of an investee and are not accounted for under the equity method of accounting are generally accounted for under Topic 321, Investments—Equity Securities. The scope of Topic 321 includes equity securities, as defined in the Master Glossary of the Codification, and other ownership interests in an entity, including investments in partnerships, unincorporated joint ventures, and limited liability companies.

2. Before the adoption of Update 2016-01, certain equity securities that did not have a readily determinable fair value and that were not accounted for under the equity method were measured at cost, less any impairments that were determined to be other than temporary. The amendments in Update 2016-01 require that an entity measure investments within the scope of Topic 321 with a readily determinable fair value at fair value, with changes in fair value included in net income each reporting period. For investments within the scope of Topic 321 without a readily determinable fair value, an entity may elect to measure those investments at their cost minus impairment (if any). Paragraph 321-10-35-2, as amended, states that if an entity identifies observable price changes in orderly transactions for the identical or a similar investment of the same issuer, it should measure the equity security at fair value as of the date that the observable transaction occurred.

3. Topic 323, Investments—Equity Method and Joint Ventures, provides guidance on the equity method of accounting, which applies to investments in common stock or in-substance common stock (or both), including common stock of corporate joint ventures. The equity method of accounting is applied when an investor has the ability to exercise significant influence over the operating and financial policies of an investee. Topic 323 does not apply to investments accounted for in accordance with Topic 810, Consolidation.

4. Stakeholders raised several questions about the interactions between the measurement alternative in Topic 321 and the equity method of accounting in Topic 323. Stakeholders noted that the measurement alternative was introduced by Update 2016-01 and that, in certain instances, diversity in its application has emerged in practice when applying and discontinuing the equity method of accounting. Furthermore, stakeholders noted that they expect the frequency of these circumstances to increase as more entities adopt the amendments in Update 2016-01 and apply the measurement alternative.

5. Stakeholders also raised questions about the interactions between Topic 321, Topic 323, and Topic 815, Derivatives and Hedging, related to the application of the guidance for certain forward contracts and purchased options to purchase securities within the scope of Topic 321. Topic 815 provides guidance on the accounting for forward contracts and purchased options that have all of the characteristics in paragraph 815-10-15-141, including the characteristic that the contract is entered into to purchase securities that *will* be accounted for under either Topic 320, Investments—Debt and Equity Securities, or Topic 321. Stakeholders noted that diverse views have emerged about the accounting for forward contracts and purchased options on securities that, upon settlement of the forward contract or exercise of the purchased option, would be accounted for under the equity method. Specifically, those stakeholders questioned whether these forward contracts and purchased options should be accounted for in accordance with Topic 321 or another Topic.

6. On May 8, 2019, the Board added this narrow-scope project to the EITF agenda to clarify certain interactions between Topic 321, Topic 323, and Topic 815.

Issues

7. The following issues were included in Issue Summary No. 1, dated May 30, 2019, and were discussed at the June 13, 2019 EITF meeting:

- Issue 1: Accounting for equity securities upon the application and discontinuation of the equity method of accounting
- Issue 2: Recognizing investee losses when an investor has other equity investments in the investee
- Issue 3: Scope considerations for certain forward contracts and purchased call options on equity securities.

Current EITF Discussion

Issue 1: Accounting for Certain Equity Securities upon the Application or Discontinuation of the Equity Method of Accounting

8. An increase in the investment in an investee that was not previously accounted for under the equity method may result in a required change in accounting to the equity method for the investor. For example, an investor acquiring additional voting stock of the investee, the investee acquiring or retiring voting stock, or other capital transactions may result in the investor obtaining significant influence over the investee. Similarly, a decrease in the investment in an investee that was previously accounted for under the equity method may result in the discontinuance of the equity method for the investor. For example, an investor's sale of a portion of an investment in the investee, sale of additional stock by the investee, or other capital transactions may result in the investor losing significant influence over the investee.

9. Stakeholders asked whether an observable transaction that results in an investor gaining (or losing) significant influence over the investee and, therefore, results in the investor applying (or discontinuing) the equity method should be considered for purposes of applying the measurement alternative in Topic 321. That is, should an investor remeasure its equity security in accordance

with the measurement alternative upon the application or discontinuance of the equity method due to an observable transaction?

10. The Task Force reached a consensus-for-exposure that an entity should consider observable transactions that would require an investor to apply (or discontinue) the equity method of accounting for the purposes of applying the measurement alternative under Topic 321 immediately before applying (or upon discontinuing) the equity method.

11. In reaching its consensus-for-exposure, the Task Force considered the Board's basis for conclusions in Update 2016-01 in which the Board noted that equity securities not accounted for under the equity method of accounting should be measured at fair value through earnings because fair value is a more relevant measurement attribute for equity investments and would be a benefit to financial statement users. On that basis, the Task Force determined that an equity security accounted for in accordance with the measurement alternative should be measured at fair value upon the occurrence of an observable transaction that results in an investor applying or discontinuing the equity method. The Task Force observed that disregarding an observable transaction related to changing measurement methodologies (that is, the application or discontinuation of the equity method) is not consistent with the Board's intent when it issued Update 2016-01. The Task Force also noted that its consensus-for-exposure would align with the accounting for equity securities with readily determinable fair values, which in practice are remeasured immediately before applying and upon discontinuing the equity method. The Task Force also decided to clarify this accounting in the Codification.

12. The Task Force also determined that remeasuring an equity security before applying (or upon discontinuing) the equity method of accounting would provide users with the most decision-useful information.

Issue 2: Recognizing Investee Losses When an Investor Has Other Equity Investments in the Investee

13. The Task Force was unable to reach a consensus-for-exposure on whether to require accumulated equity method losses that have not been allocated to an investor's investments in the investee (that is, accumulated investee losses in the memo account) to be offset against any unrealized gains resulting from remeasurement of the investments due to an observable transaction in accordance with the measurement alternative in Topic 321. Task Force members expressed different views about whether investments related to an equity method investee should be accounted for as separate or combined units of account, and if the investments are considered a combined unit of account, the sequence of applying equity method losses and unrealized gains to the other investments. Task Force members expressed uncertainty about the pervasiveness of situations in which (a) an investor has additional investments in an equity method investee that do not qualify for the equity method of accounting and (b) the investee's equity method losses have resulted in a zero carrying amount for the investor's equity method investment. The Task Force decided to remove this issue from the scope of Issue 19-A and recommended that the staff perform additional research on the pervasiveness of these situations.

Issue 3: Scope Considerations for Forward Contracts and Purchased Options on Certain Securities

14. The scope of Topic 321 includes equity securities that, as defined in the Master Glossary and amended by Update 2016-01, include rights to acquire an ownership interest in an entity at a fixed or determinable price (for example, forward purchase contracts and call options). The scope of Topic 321 excludes, among other items, (a) investments accounted for under the equity method in Topic 323 and (b) derivative instruments that are within the scope of Topic 815.

15. Topic 321 also notes that certain forward contracts and purchased options that are not derivative instruments subject to Topic 815, but that involve the acquisition of securities that will be accounted for under Topic 321, are accounted for in accordance with the Certain Contracts on Debt and Equity Securities Subsections of Subtopic 815-10. For those forward contracts and purchased options that are within the scope of Subtopic 815-10 to purchase securities within the scope of Topic 321, the guidance requires that those contracts be measured at fair value in a manner consistent with the guidance in Topic 321.

16. The guidance in the Certain Contracts on Debt and Equity Securities Subsections of Subtopic 815-10 applies only to those forward contracts and purchased options that have all of the characteristics in paragraph 815-10-15-141. The characteristic in paragraph 815-10-15-141(a) states that the contract is entered into to purchase securities that will be accounted for under either Topic 320 or Topic 321.

17. Stakeholders questioned the interaction of the scope guidance in Topic 321, Topic 323, and Topic 815 for forward contracts and purchased options on securities that, upon settlement or exercise, will be accounted for under the equity method of accounting. Specifically, those stakeholders questioned whether those forward contracts and purchased options would be outside the scope of Subtopic 815-10 because the underlying securities would not be within the scope of Topic 321 upon the settlement of the forward contract or exercise of the purchased option (that is, the contract does not meet characteristic (a) in paragraph 815-10-15-141).

18. The Task Force reached a consensus-for-exposure that an entity should not consider whether, upon the settlement of the forward contract or exercise of the purchased option, the underlying securities would, individually or with existing investments, be accounted for under the equity method for purposes of evaluating characteristic (a) in paragraph 815-10-15-141.

19. In reaching this consensus-for-exposure, the Task Force considered that entities are required to disregard any potential voting privileges that may become available to holders of securities of an investee when evaluating the requirements to qualify for the equity method in Topic 323. Furthermore, the Task Force concluded that a requirement to consider whether the securities underlying the forward contract or purchased option would be accounted for under the equity method could result in additional complexities in applying the guidance. For example, continuously determining whether an entity would have significant influence over the investee upon settlement of a forward contract or exercise of a purchased option could be complex and operationally burdensome because of changes in the capital structure of the investee.

20. Additionally, the Task Force noted that if the forward contracts or purchased options are measured under the equity method of accounting or another cost method, those instruments would

be recorded at their initial cost. Generally, at-the-money forward contracts have no cost, or a de minimis cost. For at-the-money purchased options, a premium may be paid to the option writer, but those amounts are generally insignificant compared with the total amount of the purchased securities. As such, the measurement of those forward contracts and purchased options likely would be insignificant while the economics of those instruments potentially could be significant.

21. One Task Force member indicated that the consensus-for-exposure could result in an acquirer being required to measure a forward purchase agreement (or contingent forward purchase agreement) for a controlling financial interest in the acquiree at fair value. That Task Force member noted that practice, in general, has not accounted for these contracts at fair value and that, therefore, the amendments in the proposed Update resulting from this Issue would change practice for those contracts. However, the Task Force noted that the scope of the proposed amendments resulting from this Issue should clarify, and be limited to, circumstances for which the underlying securities, upon settlement of the forward contract or exercise of the purchased option, individually or with existing investments, would be accounted for under the equity method. The Task Force determined that those proposed amendments would not result in a change in practice for the acquirer's accounting for forward contracts to purchase a controlling financial interest in an acquiree.

Effective Date and Transition

22. The Task Force did not propose an effective date for the amendments in the proposed Update resulting from this Issue or decide on the ability to early adopt those proposed amendments. Consequently, the Task Force will consider the comments received on the proposed amendments before determining when those amendments would be effective and whether to permit early adoption.

23. The Task Force reached a consensus-for-exposure that would require that an entity apply the amendments in the proposed Update resulting from this Issue prospectively. In reaching its consensus-for-exposure, the Task Force considered requiring retrospective or modified retrospective application but decided that adjusting the cost basis of an equity method investment for which an entity previously applied the measurement alternative before applying the equity method could be operationally challenging for some financial statement preparers. The Task Force also determined that remeasuring an equity security (including a forward contract or purchased option) to a previous observable transaction would result in a current-period adjustment for a historical fair value measurement that may not be indicative of the current fair value of the equity security and, therefore, may not provide decision-useful information to financial statement users.

24. The Task Force reached a consensus-for-exposure not to require any additional recurring disclosures related to equity method investments or equity securities that are accounted for under the measurement alternative because of the limited scope of the amendments in the proposed Update resulting from this Issue. The Task Force also reached a consensus-for-exposure to require that an entity disclose in the period of adoption the nature of and reasons for the change in accounting principle, the transition method, and a qualitative description of the financial statement line items affected by the change.

Board Ratification

25. At its June 26, 2019 meeting, the Board ratified the consensus-for-exposure reached by the Task Force on this Issue and directed the FASB staff to draft a proposed Update reflecting the consensus-for-exposure for vote by written ballot.

Status

26. Upon issuance of the proposed Update, a 30-day comment period will commence. Further discussion is expected at a future EITF meeting.

Issue No. 19-B

Title: Revenue Recognition—Contract Modifications of Licenses of Intellectual Property

Date Discussed: June 13, 2019

Background

1. The core principle for revenue recognition in Topic 606, Revenue from Contracts with Customers, is to recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for transferring control of those goods or services. Topic 606 provides implementation guidance on revenue recognition for licenses of intellectual property (IP) because the nature of licensing arrangements can make it difficult to determine when control of the license has been transferred to a customer.

2. A license establishes a customer's rights to the IP (such as software, franchises, trademarks, and motion pictures) of an entity. Topic 606 includes implementation guidance for licensing arrangements in paragraphs 606-10-55-54 through 55-65B and provides that, depending on the nature of the IP to which the customer will have rights, the IP is either functional IP (a right to use) or symbolic IP (a right of access).

3. An entity's promise to grant a customer a license to symbolic IP (that is, a right to access the entity's IP) includes supporting or maintaining that IP during the license period. Therefore, the nature of the entity's promise to the customer is both to (a) grant the customer rights to use and benefit from the entity's IP and make that underlying IP available for the customer's use and benefit and (b) support or maintain the IP during the license period (or over the remaining economic life of the IP, if shorter). Consequently, the customer will simultaneously receive and consume the benefit from the entity's performance as the performance occurs, and the criterion in paragraph 606-10-25-27(a) for revenue recognition over time will be met.

4. A license to functional IP provides a customer with a right to use an entity's IP as it exists at the point in time when the license is granted. The entity's promise to provide the customer with a license to functional IP (or the right to use its IP) is satisfied at the point in time when the customer obtains the control of the license (per paragraph 606-10-25-30).

Revenue recognition for license renewals

5. Under paragraph 606-10-55-58C revenue from a license of IP cannot be recognized before (a) an entity provides (or otherwise makes available) a copy of the IP to the customer and (b) the beginning of the period during which the customer is able to use and benefit from its right to access or its right to use the IP. Paragraph 606-10-55-58C also specifies that an entity should recognize revenue from a license renewal no earlier than the beginning of the renewal period.

Contract modification guidance

6. Topic 606 includes guidance on determining how to account for contract modifications. A contract modification is defined in Topic 606 as a change in the price or scope of the contract. Analysis of whether the additional goods or services are distinct and whether the pricing of the

modification is consistent with the standalone selling price (SSP) of the additional goods or services determines how to account for the modification.

7. Paragraph 606-10-25-12 requires a contract modification to be accounted for as a separate contract when distinct goods or services are added and the increase in the price of the contract reflects the entity's SSP of those additional goods or services adjusted to reflect the circumstances of the contract.

8. If the modification does not result in a separate contract, paragraph 606-10-25-13 is applied to determine whether the modification is (a) the termination of the existing contract and the creation of a new contract, (b) a part of the existing contract, or (c) a combination of both.

Contract modifications involving licenses of IP

9. A modification of a license of IP may include an extension to the term of the original license along with other changes (for example, adding or removing other goods or services from the contract or changing the pricing of the original license of IP granted to the customer). Stakeholders have highlighted diversity in practice in how modifications of licensing arrangements are accounted for under Topic 606.

10. On May 8, 2019, the Board added this new narrow scope Issue to the EITF agenda to address revenue recognition for contract modifications of licenses of intellectual property, which will primarily affect licenses to functional IP.

Issues

11. The following issues were included in Issue Summary No. 1, dated May 30, 2019, and were discussed at the June 13, 2019 EITF meeting:

- Issue 1: Accounting for contract modifications under which the contract term for existing rights is extended, while also adding rights
- Issue 2: Accounting for the revocation of licensing rights (including conversion of term software licenses to SaaS [software as a service] arrangements).

Issues 1 and 2 were discussed at the June 2019 meeting but no technical decisions were made.

Current EITF Discussion

12. At the June 13, 2019 EITF meeting, the staff provided the Task Force with background on Topic 606, introduced the underlying issues, and provided analysis of the preliminary alternatives. The Task Force was not asked to reach any conclusions at this time.

Issue 1: Accounting for Contractual Modifications under Which the Contract Term for Existing Rights Is Extended, While Also Adding Rights

13. This issue relates to the accounting for contract modifications involving licenses of IP that extend the original license term and grant additional rights. There is diversity in the application and interpretation of contract modification guidance and licensing guidance in cases in which a modification to a license arrangement involves extensions of the original license term and granting

additional rights to the licensee (that is, the renewal is not at the *same* terms and conditions as the original licenses). The diversity primarily results from different views about whether revenue resulting from the modification should be recognized at the date of the modification (because the modification is accounted for as the termination of the existing contract and the creation of a new contract) or at the start of the renewal period (because of the guidance on license renewals).

14. In discussing the potential alternatives in Issue Summary No. 1, one Task Force member noted that until the issuance of Accounting Standards Update No. 2016-10, *Revenue from Contracts with Customers (Topic 606): Identifying Performance Obligations and Licensing*, which added the renewals guidance, the FASB's accounting guidance on revenue recognition was converged with the IASB's revenue recognition guidance. That Task Force member asked whether the FASB staff had considered removing the renewals guidance as an alternative, and the staff noted that removing the renewals guidance was not a potential alternative because the amendment in Update 2016-10 was intended to reduce diversity and therefore removing that guidance would reintroduce the diversity that existed prior to the issuance of that Update.

15. Another Task Force member requested that if a Working Group is formed, as recommended by the FASB staff, participants be given materials related to the Board's decisions that resulted in Update 2016-10. That Task Force member noted that those materials would help the Working Group as it discusses the potential alternatives. One Task Force member also indicated that the Working Group should include participants from industries outside the software industry.

Issue 2: Accounting for the Revocation of Licensing Rights (Including Conversion of Term Software Licenses to SaaS Arrangements)

16. An emerging issue in the software industry is the existence of contracts that include, whether from inception or by subsequent modification, a feature that allows a customer to convert from an on-premise software license to a hosted software solution (such as SaaS arrangements). Revenue from a license to functional IP is recognized at a point in time when the entity provides a copy of the IP to the customer and the period in which the customer is able to use and benefit from the license has begun. Revenue from SaaS arrangements is typically recognized over time because the performance obligation likely would meet the criteria for over time recognition. Therefore, questions have arisen about how to account for the conversion of a point-in-time license to a service provided over time.

17. One Task Force member noted that similar situations exist in the healthcare and pharmaceutical industries. Specifically, these industries deal with chargebacks and returns that can be a significant portion of the reconciliation of gross sales to net sales. That Task Force member asked the staff to look at how this Issue may affect those industries.

18. Some Task Force members noted that when developing the existing guidance on accounting for licenses and SaaS arrangements, there was an emphasis on consistency between the accounting from the vendor's perspective and the customer's perspective. Those Task Force members suggested that the FASB staff consider the customer's perspective as it develops the alternatives.

19. One Task Force member encouraged the staff to consider the economics of the transaction (for example, pricing structures and options) and how the potential alternatives would reflect those economics.

20. A Task Force member suggested that the staff consider another potential alternative under which the term of the license is considered to be one day, so the entity would only recognize revenue for that day. That Task Force member stated that this alternative would remove many of the complexities associated with the issue.

Status

On July 16, 2019, the FASB held a nonpublic Working Group meeting to gather feedback and further develop the alternatives for this Issue. The Working Group's feedback will be reported in an issue summary supplement. Further discussion is expected at a future EITF meeting.