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November 4, 2020

Hillary H. Salo
Technical Director
Financial Accounting Standards Board
401 Merritt 7, PO Box 5116
Norwalk, CT 06856-5116

Via Email to director@fasb.org

Re: File reference No. 2020-600

Dear Ms. Salo:

Grant Thornton LLP appreciates the opportunity to comment on proposed Accounting Standards Update (ASU), *Franchisors – Revenue from Contracts with Customers: Practical Expedient*.

We acknowledge the Board's responsiveness and attention to address concerns raised by stakeholders with respect to accounting for initial franchise fees, including the efforts to date by both the Board and staff on published educational materials and outreach with industry stakeholders.

While we support reducing the cost and complexity of applying ASC 606 to initial franchise fees for nonpublic franchisors, we are not certain that the proposed amendments achieve that objective. This letter highlights areas where we believe the proposed amendments may introduce additional complexity and provides our recommendations for addressing that complexity.

Perhaps most importantly, we are concerned that the proposed ASU sets a precedent of the FASB's willingness to issue further industry-specific guidance. This would seem to contradict one of the original goals of ASC 606, which was to develop a common revenue standard for U.S. GAAP and IFRS that entities could apply consistently across industries. We acknowledge that the application of Step 2 in the revenue recognition standard may require significant judgment for nonpublic franchisors, but, in our experience, the same can be said for many other entities across many industries – both public and nonpublic.



We expand on these comments and provide considerations and recommendations in the paragraphs that follow.

Responses to Invitation to Comment questions

Question 1: Do you support introducing guidance for franchisors that are not public business entities to account for pre-opening services provided to a franchisee? Please explain why or why not.

The summary of the proposed ASU notes, in part, that the amendments in the proposed ASU "...are intended to reduce the **cost and complexity** of applying Topic 606 to initial franchise fees for franchisors that are not public business entities by providing a practical expedient for applying Topic 606 to initial franchise fees" [emphasis added].

We think that the proposed amendments may simplify the application of Step 2 in ASC 606 for nonpublic franchisors, but only for simple and straightforward franchise agreements (for example, those where pre-opening services are clearly within the scope of the amendments and end prior to or when the store opens). We believe that most franchise agreements are not so simple and are therefore concerned that the proposed guidance would introduce additional complexity if finalized without additional clarification. We further discuss this potential complexity in our response to Question 3.

We are also concerned that the proposed ASU sets a precedent to issue further industry-specific guidance, which, as previously noted, would contradict one of the original goals of ASC 606. We observe that the application of Step 2 remains a complex exercise for management at companies in a number of other industries where contracts typically involve a license and related goods or services (for example, information technology). We could envision other industries requesting similar relief from the FASB if relief is provided in any form to a select group of entities.

Question 2: Should the scope of the amendments in this proposed Update be limited to franchisors that are not public business entities? Alternatively, would it be appropriate for entities in other industries with comparable arrangements that are not within the scope of the proposed Update to analogize to the amendments? Please explain why.

We believe that the scope of the amendments in the proposed ASU, including our suggestions incorporated in this letter for clarifying and improving the amendments, should be limited to franchisors that are not public business entities, as described in ASC 952-606-15-2. Further, we agree that entities should not analogize to the proposed amendments to account for comparable arrangements in other industries, as described in ASC 952-606-15-3. As stated above, we are concerned that the proposed amendments could set a precedent whereby entities in other industries will seek to obtain relief, including by analogy if the proposed ASU is silent on entities' ability to analogize to the guidance. We are in favor of limiting any further deviations from ASC 606's universal accounting model by requiring entities in other industries seeking relief to go through the formal standard-setting process.



Question 3: Would the proposed amendments to simplify Step 2 – identify the performance obligations – reduce the cost and complexity of applying Topic 606 to pre-opening services? Please explain why or why not.

In straightforward circumstances, we believe that the proposed amendments may help to reduce the cost and complexity of applying ASC 606 to pre-opening services (for example, for franchisors whose pre-opening services squarely align with the list included in ASC 952-606-25-2 and are completed prior to the store opening). We believe that many, if not most, franchise agreements are not so straightforward, however, and that entities may find that the proposed amendments introduce additional complexity and raise additional questions.

For example, consider the following questions:

- a. How should a nonpublic franchisor account for services that occur both in the pre-opening and post-opening time periods? For example, the franchisor may provide training to franchisee personnel during the pre-opening period and agree to provide ongoing training on a quarterly basis after the store has opened. Similarly, the franchisor may provide bookkeeping services that begin during the pre-opening period but end four months (or longer) after the store opens. Should the franchisor bifurcate such services between the pre-opening and post-opening periods? Are those services excluded from the scope of the amendments because they are not completed in their entirety prior to the opening? The Board may consider clarifying the accounting for such services, perhaps in part by providing a glossary definition of “pre-opening services.” See further discussion in the Appendix.
- b. How do nonpublic franchisors account for renewal rights? We acknowledge that paragraph 31 in the Basis for Conclusions (BC31) in the proposed ASU explains the logic behind excluding renewal rights from the scope of this project; however, assessing renewal rights and determining whether a renewal right constitutes a material right can be an area of significant judgment and may therefore be costly and complex. Further, we are concerned that nonpublic franchisors will assume they do not need to consider whether renewal rights constitute a separate performance obligation if the proposed amendments are finalized without clarification. Because the purpose of the proposed amendments is to simplify Step 2 in the revenue recognition model, we encourage the Board to address Step 2 in its entirety, including how nonpublic franchisors should consider renewal rights.
- c. Will nonpublic franchisors experience additional complexity in determining whether it is probable that continuing franchise fees will cover the cost plus a reasonable profit on providing the continuing services in accordance with ASC 952-606-25-3? How do renewals factor into this assessment? The proposed amendments do not define the period over which the reasonable profit should be considered or whether the proposed guidance means “at all times” or is based on a single cumulative estimate of profit over the franchise license term taken as a whole.



Question 4: In paragraph 952-606-25-3, the proposed amendments would reinstate superseded guidance from paragraph 952-605-25-4 as a required criterion for applying the practical expedient. Is this guidance operable? Please explain why or why not.

While the proposed amendments would reinstate guidance eliminated from the Codification, the introduction of the concept of a “symbolic license” changes the way entities evaluate their arrangements to ensure they can apply the practical expedient offered under the proposed guidance. We believe that start-up franchisors may have difficulty determining whether it is probable that the continuing fee will cover the cost of the continuing services, including the symbolic license, to be provided by the franchisor plus a reasonable profit on the continuing services. We recommend that the Board considers:

- Addressing that the continuing services now include a symbolic license, which was not a factor under ASC 952-605
- Expanding on Example 1, Case B to provide considerations for making this evaluation

Question 5: Should the scope of the proposed amendments be limited to pre-opening services? If not, please explain why.

Yes.

Question 6: Is additional guidance about other aspects of applying Topic 606 to pre-opening services needed for the proposed amendments to be operable? If so, what specific guidance is needed?

See recommendations in our response to Question 3.

Question 7: Should entities that elect to apply the practical expedient be required to disclose that fact? Do the proposed amendments provide decision-useful information for users of financial statements? If not, please explain why.

We believe that entities should be required to disclose their use of the practical expedient, consistent with the requirement to disclose their use of other practical expedients in ASC 606.

We defer to financial statement users on the decision-usefulness of the information provided.

Question 8: Should entities that have not yet adopted Topic 606 be required to apply the transition provisions and effective date in paragraph 606-10-65-1 to the proposed amendments? If not, please explain why.

Yes.



Question 9: Should entities that have already adopted Topic 606 be required to apply the proposed amendments on a full retrospective basis, including an entity's first reporting period under Topic 606? If not, please explain why.

No. We believe providing an option to apply the proposed amendments on a full retrospective basis or prospective basis to all new franchise agreements would be consistent with the stated purpose of simplifying the application of ASC 606 for nonpublic franchisors.

Question 10: For entities that have already adopted Topic 606, should the proposed amendments be effective for annual reporting periods beginning after December 15, 2020, including interim reporting periods within that period, with early application permitted? If not, please explain why.

Yes.

We would be pleased to discuss our comments with you. If you have any questions, please contact Lynne Triplett, Partner (lynne.triplett@us.gt.com), or Susan Mercier, Partner (susan.mercier@us.gt.com).

Sincerely,

/s/ Grant Thornton LLP

Appendix

Other comments for consideration

1. The stated intention of the proposed ASU (on page 1 of the Summary) is to “...*reduce the cost* and complexity of applying Topic 606 to initial franchise fees for franchisors that are not public entities...[emphasis added].” We note that the least costly alternative would be to provide an option for entities to recognize the entire initial franchise fee over the term of the franchise agreement.
2. Pre-opening services:
 - a. Consider defining “pre-opening services.” For example, if a franchisor provides bookkeeping services prior to the store opening as well as ongoing bookkeeping services, would (1) all bookkeeping services be subject to the practical expedient, (2) none of the services be subject to the expedient because they are not completed in their entirety prior to the store opening, or (3) all bookkeeping services be bifurcated based on those performed before and after the store opening?
 - b. ASC 952-606-25-2 says, “...**the** following pre-opening services...[emphasis added].” The wording does *not* say “such as,” “consistent with,” or another appropriate phrase. Accordingly, we recommend deleting “consistent with” from BC13 and ASC 952-606-55-6 to avoid any misinterpretation that the list in ASC 952-606-25-2 is not all-inclusive.
 - c. We appreciate why the Board reinstated the list in ASC 952-606-25-2 and understand that it is operable as demonstrated by franchisors’ use of this list in the past. That said, we are concerned about the relevance of the list as business practices evolve in the future and recommend that the Board consider making the items on the list more evergreen.
3. BC19 references the shipping and handling election in ASC 606-10-25-18A. We recommend changing this to ASC 606-10-25-18B.
4. The term “initial franchise fees” is not defined, but is used throughout the proposed amendments. Due to its significance in the proposed ASU, we recommend that the term be defined in the Master Glossary to ensure consistent interpretation and application.
5. BC15 notes that a “practical expedient” is defined in the Private Company Council Framework as “...a more cost-effective way of achieving the *same or similar accounting* or reporting objective.” Further, we note that the summary of the proposed ASU states that “...the Board expects...applying the practical expedient will result in accounting results *generally consistent* with the intent of Topic 606 for those entities” [emphasis added].



We suggest removing this wording in the Summary as it could be misconstrued as indicating that those entities (such as public company franchisors) currently applying ASC 606 as written should be getting to the same or similar accounting as that provided for in these proposed amendments.