



November 5, 2020

Ms. Hillary H. Salo
Technical Director
Financial Accounting Standards Board
401 Merritt 7
Norwalk, Connecticut 06856-5116

Re: Proposed Accounting Standards Update, *Revenue from Contracts with Customers (Subtopic 952- 606)* – Practical Expedient
Your File Reference No. 2020-600

Dear Ms. Salo:

The International Franchise Association (IFA), the world’s oldest and largest organization representing franchising, is pleased to submit this response to the FASB’s discussion draft. In particular, we are pleased to continue the dialogue with the FASB and its staff by providing these comments.

IFA responds on behalf of the nation’s franchising community, which before the COVID-19 pandemic, was comprised of over 733,000 establishments that employed nearly 8 million individuals and contributed \$674.4 billion of economic output to the U.S. economy. In this period of unprecedented economic stress, we especially appreciate the FASB’s willingness to consider technical clarifications that have the effect of reducing the compliance cost to small businesses, such as franchisors.

We appreciate all of the efforts of the FASB and staff in response to concerns raised by those in the franchise sector in the adoption and implementation of Accounting Standards Codification 606, *Revenue from Contracts with Customers* (“ASC 606”). We concur with the Board’s assessment with regard to the issues raised by primarily franchise-related stakeholders who expressed concerns about the level of effort required to account for initial franchise fees by private company franchisors and the accounting outcome of deferring some or all of the initial franchise fee over the franchise license term. We are also appreciative that the Board addressed the concern that some entities that are not public business entities appeared to presume that the initial franchise fee would always be recognized over the license term rather than applying the Topic 606 model to identify performance obligations.

As an association representing the franchise sector, which includes many franchisors that are start-ups or that have a small number of franchise units, we support the Board’s proposed practical expedient, *Proposed Accounting Standards Update, Revenue from Contracts with Customers (Subtopic 952- 606) Practical Expedient*, intended to facilitate reducing the cost and complexity of applying Topic 606 to initial franchise fees for franchisors that are not public business entities.

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In conjunction with our support please refer to our comments and responses to the following 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.

We support the introduction of this guidance.

In assessing whether an entity's promises to transfer goods or services to the customer are separately identifiable, in accordance with paragraph 606-10-25-19(b), the objective is to determine whether the nature of the promise, within the context of the contract, is to transfer each of those goods or services individually or, instead, to transfer a combined item or items to which the promised goods or services are inputs. Franchisors by nature, provide substantial pre-opening services related to the specific franchise concept to be opened. The franchisee's expectation is for the franchisor to provide them with various training and guidance before opening, as well as additional on-going training. As it relates to each of the individual promises comprising the Pre-Opening Activities, the franchisor typically concludes that certain services are capable of being distinct by themselves in accordance with ASC 606-10-25-19a and 19b.

The time and cost that franchisors expend in undertaking this analysis of the distinction of services varies considerably by franchisor and by franchise concept. Moreover, different subjective judgments made lead to different results among franchisors that offer virtually the same pre-opening services to their respective franchisees. This wide-ranging analysis leads to results that hinder the comparability among various franchise concepts, potentially making it harder for a prospective franchisee to compare financial statements issued by different franchisors in the same sector. Moreover, the resources spent on conducting the analysis of individual pre-opening services as distinct obligations fail to result in useful comparative financial statements, meaning that the added time and accounting fees, and in turn audit fees, devoted to that exercise result in little benefit to the parties that consume the results.

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.

Although the IFA represents the franchising sector and is appreciative of the proposed guidance as it applies to franchisors, we do support that the scope amendments be applicable to other industries where the subjective conclusions have the ability to create uncertainty when considering comparability between like entities.

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.

As an association, we have received feedback from franchisors as well as from accounting service providers within the franchise community that has consistently expressed concern as to

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the extensive costs both as to the time spent as well as actual costs incurred internally and externally to analyze and identify services to the customer that are separately identifiable, in accordance with paragraph 606-10-25-19 (b).

We have observed among our members and throughout the franchise sector that, because of the anticipated extensive costs and subjectivity related to the required analysis of separately identifying obligations, that a fair number of financial statements reflect a presumption that the initial franchise fee should be fully deferred. We note this practice and observe that it runs directly contrary to the salient point expressed by Board Member Christine Botosan, who stated that it would be just as wrong to defer fees that should be recognized immediately as it would be to recognize immediately fees that should be deferred.

We believe that the simplicity of implementing the practical expedient will alleviate the need to analyze and differentiate the various pre-opening obligations provided by a franchisor classified as distinct or not, thus saving a large portion of the costs, time consumed, as well as subjectivity experienced specifically when associating an initial franchise fee received by the franchisor.

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.

We agree that the guidance in paragraph 952-606-25-3 (the proposed amendments to reinstate superseded guidance from paragraph 952-605-25-4 as a required criterion for applying the practical expedient) would be operable. However, the detail listing in 952-606-25-2, may not be all inclusive and should be explained as an example of the types of costs categorized as pre-opening, so as not to be viewed as a potential finite listing.

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

We believe that the proposed amendments for the practical expedient will alleviate a large portion of the costs, time consumed, as well as subjectivity experienced specifically when associating an initial franchise fee received by the franchisor. We believe that it is appropriate to limit the scope of the amendments to services that franchisors provide before, at the same time as, or in conjunction with opening a new franchised business.

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?

The proposed guidance addresses three concerns with regard to the application of ASC 606 within the franchise industry: (1) costs; (2) subjectivity; and (3) the lack of comparability amongst franchisors adopting the standard. We believe that these concerns are predominant in the franchise industry, including both publicly-traded entities as well as non-public entities.

Although the codification is explicit as to the requirement under ASC 606-10-25-19a and 19b, that there is no presumed justification to forgo step 2 and defer the entire initial franchise fee.

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Indeed, many franchisors and their outside audit professionals have incorrectly presumed that full deferral of pre-opening costs is required under the standard (most likely on the assumption that the goods or services are so interdependent or interrelated with the ongoing access to the license and its term as to mandate that conclusion). Additional guidance with regard to clarification of what constitutes the goods or services that are highly interdependent or highly interrelated, along with potential examples, would be helpful in defining the FASB intention and expectations, in line with adoption of ASC 606.

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 do not believe that additional disclosure is necessary to provide the reader with an understanding of how the franchisor has elected to comply with ASC 606. The disclosures that franchisors already provide with regard to the adoption of ASC 606 are extensive and provide the reader with sufficient information to fully understand the firm's conclusions and the impact of the adoption. If the FASB concludes that additional disclosure is appropriate or simply preferable, we would recommend that it be simple and straightforward, so as not to add to the burden of adopting ASC 606, which is a key goal of considering the practical expedient.

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.

We believe that entities that have not yet adopted should be given the option of adopting a modified retrospective transition or full retrospective transition for annual reporting periods beginning after December 15, 2019, and interim reporting periods within annual reporting periods beginning after December 15, 2020.

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.

The proposed expedient states that if an entity has already adopted Topic 606, the amendments in this proposed update would be effective in interim and annual periods beginning after December 15, 2020. Early application would be permitted. For those entities, this proposed guidance would be applied retrospectively to the date Topic 606 was adopted. We agree with this proposal to accommodate the potential variations that would be reflected in the comparative financial statements. Alternatively, where feasible, a footnote reference might be an efficient way to provide useful information to the reader without having to engage in a full retrospective or restatement of the adoption year versus a modified retrospective (e.g., where a franchisor has allocated all or most of the pre-opening obligations as separate performance obligations).

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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.

The proposed expedient states that if an entity has already adopted Topic 606, the amendments in this proposed Update would be effective in interim and annual periods beginning after December 15, 2020. Early application would be permitted. For those entities, this proposed guidance would be applied retrospectively to the date Topic 606 was adopted. Although we agree with this proposal, we feel that an allowance for early adoption of the expedient would allow an entity to apply the guidance retroactively thereby creating less variations within the financial statement that may be caused primarily due to application of the guidance surrounding the standard as opposed to actual entity operations.

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Thank you for your thoughtful consideration of these concerns and important technical clarifications during this period of economic damage that challenges small concerns, including many franchisors. We remain ready to work with you and the FASB's professional staff in any way that we can be helpful.

Sincerely,



Robert Cresanti, CFE
President and CEO
International Franchise Association