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Technology Spotlight

A Few Bytes Away From Downloading the Converged Revenue Recognition Standard!

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The Bottom Line

The proposed revenue model requires management to use greater judgment in recognizing revenue and related costs and may change the timing of revenue recognition from current practice.

- On November 14, 2011, the FASB and IASB (the "boards") jointly issued their revised exposure draft (ED) *Revenue From Contracts With Customers*. The revised ED proposes a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers and would supersede most current revenue recognition guidance. In addition, on January 4, 2012, the FASB issued a companion proposed ASU for public comment that would codify the revised ED's amendments.
- The revised ED would supersede ASC 985-605[1] (formerly SOP 97-2[2]) in its entirety. The elimination of the requirement for vendor-specific objective evidence (VSOE) of fair value may significantly modify the timing of revenue recognition for software entities.
- Warranties that provide a service in addition to simple assurance that a product complies with agreed-upon specifications must be treated as separate performance obligations, thereby potentially delaying the recognition of a portion of revenue until the obligations are satisfied.
- Under the revised ED, the determination of whether virtual goods and services are transferred at a point in time or over a period of time may significantly affect revenue recognition.
- Comments on the revised ED and the FASB companion proposed ASU are due by March 13, 2012. A final revenue recognition standard is not expected to be issued until later in 2012 and would not be effective earlier than for annual periods beginning on or after January 1, 2015.

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

[2] AICPA Statement of Position 97-2, *Software Revenue Recognition*.

Beyond the Bottom Line

This *Technology Spotlight* highlights the framework of the proposed revenue recognition model and the potential implications for technology companies.

Background

The revised ED states that the goal of the boards' revenue recognition project, which began in 2002, is to "clarify the principles for recognizing revenue and to develop a common revenue standard for U.S. GAAP and IFRSs." After receiving nearly 1,000 comment letters and redeliberating almost every aspect of their June 2010 ED, the boards modified the proposed guidance and developed the revised ED (changes from the June 2010 ED are discussed in detail in Deloitte's November 15, 2011, *Heads Up*). The revised ED retained the overall model that was originally proposed, which outlined five sequential steps to recognizing revenue:

1. "Identify the contract with a customer."
2. "Identify the separate performance obligations in the contract."
3. "Determine the transaction price."
4. "Allocate the transaction price to the separate performance obligations in the contract."
5. "Recognize revenue when (or as) the entity satisfies a performance obligation."

The proposed model requires technology entities to reassess their accounting for various software and hardware products and services and determine whether accounting changes are necessary.

The revised ED states that the core principle for revenue recognition is that an "entity shall 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 those goods or services." Although the boards did not modify the five steps to applying this principle, they did change how each step is applied as well as other aspects of the proposed model. For instance, the proposal would require capitalization of certain costs of obtaining and fulfilling a contract and would modify the criteria for recognizing losses on certain onerous performance obligations.

Compared with current revenue recognition guidance, the revised ED requires significantly expanded disclosures about revenue recognition, including both quantitative and qualitative information about (1) the amount, timing, and uncertainty of revenue (and related cash flows) from contracts with customers; (2) the judgment, and changes in judgment, exercised in applying the proposal's provisions; and (3) assets recognized from costs to obtain or fulfill a contract with a customer.

Key Accounting Issues

The revised ED clarifies the revenue recognition principles and includes additional guidance on certain revenue transactions. Although the effect of the proposals on some entities is expected to be limited, hardware and software entities operating in the technology industry may face significant accounting and operational challenges as a result of the revised ED, a number of which are discussed below.

Software

The revised ED eliminates industry-specific software guidance, requiring that entities in all industries, including the software industry, apply a "one-size-fits-all" model. Under the revised ED, goods and services in a software contract are treated as separate performance obligations if they are deemed "distinct." The revised ED contains criteria for determining whether goods or services represent distinct performance obligations that should be accounted for separately. Revenue is allocated to each separate performance obligation on the basis of its relative stand-alone selling price. If the stand-alone selling price of a performance obligation is not observable, the entity must use one of the methods

described in the revised ED to estimate it. Revenue is then recognized for each separate performance obligation as the obligation is satisfied (either over time or at a point in time), up to the amount to which an entity is reasonably assured to be entitled.

Software companies may be most significantly affected by (1) the elimination of the requirement that VSOE of fair value must exist for an entity to separate elements in a software arrangement and (2) the change in scope of the application of the residual method for allocating the consideration to each element. The paragraphs below discuss these items and a few other differences. Also see the appendix for a detailed comparison between ASC 985-605 (formerly SOP 97-2) and the revised ED.

Elimination of VSOE Requirement

Currently, ASC 985-605 provides industry-specific guidance on accounting for multiple-element software arrangements. Under the current guidance, to separate a software arrangement that includes multiple elements, a vendor must establish VSOE of fair value, which ASC 985-605-25-6 defines as:

> a. The price charged when the same element is sold separately
>
> b. For an element not yet being sold separately, the price established by management having the relevant authority; it must be probable that the price, once established, will not change before the separate introduction of the element into the marketplace.

The elimination of VSOE and the allocation of revenue to each performance obligation on the basis of stand-alone selling prices may significantly change revenue recognition patterns in software arrangements.

The separate-sale criterion for establishing fair value is more restrictive than that in any existing literature that applies to multiple-element arrangements. Whether VSOE of fair value can be established for an element may dramatically affect how revenue is recognized in a multiple-element arrangement. Further, variations in pricing from customer to customer, the unique and customer-specific nature of many software elements, and the lack of historical sales information for new software products can often make it difficult or impossible to establish VSOE of fair value.

Because the revised ED is eliminating the VSOE requirement, revenue recognition in software contracts will no longer be limited if VSOE of fair value is not established for certain goods or services in a contract. However, while entities will no longer be required to establish and maintain processes for developing VSOE of fair value for goods or services sold in software transactions, the revised ED will still require entities to develop similar processes for determining the stand-alone selling price of each performance obligation.

Elimination of the VSOE requirement may have a significant impact on software transactions that include technology "roadmaps." Most software companies develop roadmaps to articulate both short-term and long-term goals for the future development of software sold to a customer. Roadmaps can include specific upgrades or enhancements to the functionality of software to be delivered at a specific time in the future. Because such upgrades or enhancements typically have not been developed or sold separately at contract inception, VSOE of fair value often does not exist for such elements. As described above, under current guidance, if a roadmap implies or explicitly promises the delivery of specified upgrades and VSOE of fair value does not exist for the upgrade rights, revenue related to other elements in the arrangement often must be deferred until the upgrades are delivered or VSOE of fair value is established. This limits the ability of software companies to include desired content in their product roadmaps. By replacing the separation requirement for VSOE of fair value with the concept "distinct" goods or services and requiring allocation of revenue to separate performance obligations on the basis of an estimate of stand-alone selling prices, the revised ED gives software companies more flexibility to include specified upgrade rights in their product roadmaps. In other words, revenue recognition in certain software arrangements may be accelerated as a result of the revised ED.

Residual Allocation Techniques

Multiple-element software arrangements that are not within the scope of ASC 985-605 (e.g., certain types of hosted software and data arrangements) are typically accounted for under ASC 605-25, which discusses how an entity should allocate the arrangement consideration to separate units of accounting. Entities are required, at the inception of an arrangement, to establish the "selling price" for all deliverables that qualify for separation. The manner in which "selling price" is established is based on a hierarchy of evidence that entities must consider; total arrangement consideration is allocated on the basis of the deliverables' relative selling prices. The "residual method," as described in ASC 985-605, is currently prohibited for multiple-element arrangements that are within the scope of ASC 605-25.

In the absence of observable separate sales, the revised ED requires entities to use estimates to determine the stand-alone selling price of a separate performance obligation. Although the revised ED includes three examples of suitable estimation methods, it does not prescribe one. Instead, an entity would use judgment in determining an estimation method that maximizes the use of observable inputs. The revised ED specifies that when the stand-alone selling price of a performance obligation is highly variable or uncertain, the application of a residual technique may be used as an estimation method, regardless of the type of good or service being sold.

The use of the residual technique may be permitted when the stand-alone selling price of a performance obligation is highly variably or uncertain.

Under the revised ED, an entity is permitted to apply a residual allocation technique in the circumstances described above regardless of whether the entity obtains VSOE of fair value for all other performance obligations in the arrangement (as required for arrangements that are currently within the scope of ASC 985-605). Thus, an entity might no longer need to perform or justify complex estimation techniques to determine the estimate of stand-alone selling price for highly unique goods or services in multiple-deliverable arrangements (for arrangements currently within the scope of ASC 605-25). Lastly, entities may be allowed greater flexibility in allocating revenue to performance obligations, depending on the facts and circumstances.

Overall, entities that currently find it challenging to meet the requirement for VSOE of fair value will most likely have increased flexibility to use estimates to demonstrate stand-alone selling prices and will thus be less likely to defer revenue when VSOE of fair value does not exist.

Online Gaming / New Media

Sale of Virtual Goods

Traditionally, online gaming and new media companies have charged customers a monthly subscription fee or a fee for premium services to gain access to online content for a specified period. Recently, the "free-to-play" business model has become more popular in the online industry. Under the free-to-play model, customers are given access to online content for no charge but have the option to purchase virtual goods. Virtual goods are intangible objects purchased for use in online platforms (e.g., virtual pets, avatars).

The revised ED specifies that revenue should be recognized when the entity satisfies a performance obligation by transferring a good or service to a customer and the entity is reasonably assured to be entitled to such revenue. A good or service is deemed to be transferred when the customer obtains control of that good or service, which may be over time (when certain criteria are met) or at a point in time.

A customer generally can expect a purchased virtual good to be available for use at any time. However, some contracts specify the manner in which the customer may consume the good. In certain situations, control of the virtual good may be transferred to the customer in its entirety at the point of sale so that the customer may use or consume the virtual good without any further obligation on the part of the seller to provide access to it. In this case, the revised ED would most likely require full revenue recognition for the sale of the good at the point of sale if the entity is reasonably assured to be entitled to such revenue. In contrast, in certain circumstances, a customer could be required to use a seller's online platform or other mechanism, in which case the seller would be obligated to provide further services so that the customer can use or consume the virtual good. In this case, the revised ED would most likely require revenue recognition as access to the virtual good is provided and its benefits are consumed by the customer.

Given the number of unique arrangements in this industry, online gaming and new media companies will need to consider whether their current revenue recognition practices regarding the sale of virtual goods remain consistent with the revised ED.

Breakage

The revised ED's guidance on breakage may affect the accounting for revenue related to micro-transactions in the new media and gaming industries. "Micro-transactions" occur when customers purchase virtual currency to play games, purchase virtual goods, or pay for upgrades. "Breakage" refers to the amount of virtual currency purchased by a customer that will never be spent (i.e., the virtual currency is never redeemed). In current practice, amounts related to breakage often remain classified as deferred revenue on the balance sheet until it becomes likely that the virtual currency will not be redeemed.

Entities that sell virtual goods and services may need to reconsider whether control of such goods or services is transferred at the point of sale or over a period of time.

The revised ED contains specific implementation guidance on accounting for a customer's unexercised rights (i.e., breakage). Under the revised ED, when an entity is reasonably assured of the breakage amount, such revenue is recognized in proportion to the pattern of rights exercised by the customer. If the entity is not reasonably assured of the breakage amount, such revenue would be deferred until the likelihood that the customer will redeem the virtual currency is remote.

The revised ED could modify revenue recognition related to breakage for micro-transactions. In particular, the revenue recognition related to micro-transactions may be accelerated, provided that entities have sufficient historical information to estimate the timing and amount of breakage so that they can determine that they are reasonably assured of the breakage amount.

Hardware

Currently, ASC 605-20-25-1 through 25-6 (formerly FASB Technical Bulletin 90-1[3]) provide guidance on accounting for an extended warranty that is priced and sold separately from the purchased product. Under this guidance, the invoiced amount that is paid by a customer for a separately priced warranty or maintenance contract should be recognized as revenue on a straight-line basis or in proportion to the costs expected to be incurred in performing services over the contract term.

Under the revised ED, warranties would be accounted for as follows:

- If a customer has the option to purchase a warranty separately from the entity, the entity would account for the warranty as a separate performance obligation and allocate a portion of the overall consideration to the warranty service.

[3] FASB Technical Bulletin No. 90-1, *Accounting for Separately Priced Extended Warranty and Product Maintenance Contracts.*

- If a customer does not have the option to purchase the warranty separately from the entity, the entity would use a cost accrual model to account for the warranty, unless the warranty provides a service to the customer in addition to assurance that the product complies with agreed-upon specifications (in which case the entity would account for the service as a separate performance obligation and revenue would be deferred).

Hardware entities typically provide a range of warranties on sales of products to customers. Under the revised ED, the accounting for most warranties (i.e., general warranties that are included as part of the purchase of a particular product and that assure that the good or service complies with agreed-upon specifications) under a cost accrual model will not change. However, hardware entities may wish to reassess all their warranties to ensure that there are no instances in which warranties provide any services beyond assuring that the product complies with agreed-upon specifications.

Hardware entities will need to evaluate their accounting for warranties that provide more than assurance that a product complies with the agreed-upon specifications to determine whether a separate performance obligation is embedded in the warranty. In such circumstances, hardware entities will need to gather the necessary information to allocate a portion of the transaction price to the separate performance obligation, which will affect the manner in which revenue is recorded. Hardware entities may need to further analyze warranties offering multiple services (or additional products) to identify each separate performance obligation in the arrangement. Therefore, hardware entities should thoroughly analyze all warranties that are not separately priced to determine whether they should be accounted for under the cost accrual method or whether they should be treated as separate performance obligations under the revised ED.

Warranties that provide services beyond simple assurance that a product complies with agreed-upon specifications may give rise to additional performance obligations that may alter existing revenue recognition patterns.

Select Issues That Are Likely to Affect All Technology Companies

Contract Costs

The revised ED requires capitalization of certain costs associated with obtaining a contract if those costs are incremental and recoverable. The revised ED also requires capitalization of certain costs of fulfilling a contract if all of the following criteria are met and the costs are not covered by other standards:

1. "The costs relate directly to a contract (or a specific anticipated contract)."
2. "The costs generate or enhance resources of the entity that will be used in satisfying performance obligations in the future."
3. "The costs are expected to be recovered."

Amortization of capitalized costs would occur in a manner consistent with the pattern of transfer of the goods or services to which the asset relates and, in certain circumstances, may extend beyond the original contract term with the customer (e.g., when future anticipated contracts or expected renewal periods exist). As a practical expedient, qualifying costs to obtain a contract can be expensed as incurred when the amortization period is one year or less. All capitalized-cost assets will be subject to impairment testing if any indicators of impairment exist.

Depending on how an entity currently accounts for revenue-related costs, the proposed guidance may result in significant changes in practice and potentially require technology entities to capitalize costs that they may have previously expensed. Entities may want to closely evaluate the impact of such guidance on their current accounting policies and consider the need to determine their accounting policy related to contract costs for short-term contracts with a duration of one year or less.

Presentation and Disclosures

The revised ED would require significantly more extensive disclosures than current revenue standards, including quantitative and qualitative information about contracts and the significant judgments used in applying the guidance to those contracts. Entities should consider how detailed their disclosures need to be to meet the requirements and how much emphasis to place on each disclosure requirement. The required disclosures would include:

- A disaggregation of reported revenue in the "primary categories that depict how the nature, amount, timing, and uncertainty of revenue and cash flows are affected by economic factors."
- A reconciliation of the beginning and ending balance of contract assets and liabilities.
- Certain information about performance obligations (e.g., types of goods or services, significant payment terms, typical timing of satisfying obligations, and other provisions).
- Information about onerous obligations (extent and amount of such obligations, the reasons they became onerous, the expected timing to satisfy the liability, and reconciliation of onerous balances).
- A description of the significant judgments, and changes in those judgments, that affect the amount and timing of revenue recognition.
- Information about the methods, inputs, and assumptions used to determine the transaction price and allocate amounts to performance obligations.
- Information about assets recognized from costs to obtain or fulfill a contract, including a reconciliation of the beginning and ending assets (by main category of asset).

The revised ED requires significantly more disclosures, including the judgments used in applying the guidance.

Other

The revised ED provides guidance on many other topics that were not highlighted above, including licenses and rights to use, rights of return, principal-versus-agent considerations, bill-and-hold arrangements, collectibility, onerous contracts, and customer acceptance. Technology companies should carefully analyze such guidance, since it may differ from current practice. Note that some of these topics are discussed in relation to software arrangements in the attached appendix.

Challenges for Technology Companies

Increased Use of Judgment

Management will need to exercise significant judgment in applying certain of the revised ED's requirements, including those related to the identification of performance obligations and allocation of revenue to each performance obligation. It is important for entities to consider how the revised ED specifically applies to them so that they can prepare for any changes in revenue recognition patterns.

Retrospective Application

The revised ED proposes retrospective application, with certain optional practical expedients available to entities at their discretion. This aspect of the proposal may require technology entities to gather data and assess contracts that commenced several years before the revised ED's effective date. Entities also will most likely be required to perform dual tracking of revenue balances during this retrospective period, given the potential difficulty associated with retroactively recalculating revenue balances at the time the new standard becomes effective.

Impact on Contracts

Many organizations have several business contracts that are linked to financial performance or revenue recognition specifically, such as sales compensation structure agreements. If revenue recognition changes under the revised guidance, items such as compensation plans may also need to be evaluated and adjusted accordingly.

Systems, Processes and Controls

The revised ED proposes several new practices and disclosure requirements under which technology entities will have to gather and track information that they may not have previously monitored. The systems and processes associated with such information may need to be modified to support the capture of additional data elements that may not currently be supported by legacy systems (e.g., data elements needed to determine and allocate the transaction price between separate performance obligations or elements related to contract costs that must be capitalized under the revised ED).

Regarding transaction prices, entities may need to develop a new method of establishing a stand-alone selling price for each performance obligation, taking into account (1) variable consideration, (2) the time value of money, (3) noncash consideration, and (4) consideration payable to a customer. Because an entity has not previously considered many of these factors in establishing VSOE or estimated selling prices under the current guidance, the entity will need to update its current policies and procedures to establish guidance on determining transaction prices.

Entities will need to reevaluate existing systems, processes, and controls to ensure that they are able to produce the required information under the revised guidance.

In addition, to ensure the effectiveness of internal controls over financial reporting, management will need to assess whether additional controls need to be implemented. Technology entities may need to begin aggregating essential data from new and existing contracts, since many of their existing contracts may be subject to the proposed rules given the requirement to apply the revised ED retrospectively.

Income Taxes

Tax departments need to assess changes in book revenue recognition methods to prepare for the tax effects. Federal income tax law contains specific rules on certain types of revenue, such as income from long-term contracts and advance payments for goods and services. Those rules often overlap with a taxpayer's financial reporting policies, in which case the taxpayer often applies, as its tax method, the revenue recognition method it uses in maintaining its books and records. Because the proposed guidance may change the amount and timing of revenue recognition for entities that maintain their books and records under U.S. GAAP or IFRSs, the accounting proposed in the revised ED may have cash tax implications or give rise to new book-tax differences that will need to be captured, calculated, and tracked through tax accounting processes and systems.

If a change in a tax accounting method is advantageous or expedient, including circumstances in which the book method has historically been used, the taxpayer will most likely be required to obtain approval from the tax authorities. Similar implications may arise in foreign jurisdictions that maintain statutory accounting records under U.S. GAAP or IFRSs.

Thinking Ahead

Comments on the revised ED and the FASB companion proposed ASU are due by March 13, 2012. A final standard is not expected to be issued until later in 2012 and would be effective no earlier than for annual periods beginning on or after January 1, 2015 (with a minimum of a one-year deferral for nonpublic entities applying U.S. GAAP). Technology entities should take advantage of this time to carefully examine the revised ED, provide feedback on the proposed model, and begin assessing the impact it may have on their current accounting policies, procedures, systems, and processes.

Appendix — Key Differences Between ASC 985-605 and the FASB's and IASB's Revised ED

The table below summarizes key differences between ASC 985-605 and the FASB's and IASB's revised ED. It does not address all possible fact patterns and should be read in conjunction with ASC 985-605, with the revised ED, and with other relevant guidance. ASC 985-605 states that if an arrangement contains software as well as services that involve significant production, modification, or customization of the software, the services cannot be recognized separately from the software and the arrangement is therefore within the scope of ASC 605-35. The revised ED would completely supersede ASC 985-605 and ASC 605-35, among most other current revenue recognition guidance in U.S. GAAP. The table focuses solely on the potential impacts to contracts currently within the scope of ASC 985-605 and does not address the potential changes to contracts within the scope of ASC 605-35. Although the revised ED also addresses other topics that are not in ASC 985-605, such as onerous contracts, costs to obtain or fulfill a contract, financial statement presentation, and disclosures, the table does not assess the potential impact of those topics.

The links below can be used to jump to groups of topics in the table, which consists of the five primary steps for revenue recognition under the revised ED (as well as its scope):

- Scope.
- Step 1: Identify the Contract With a Customer.
- Step 2: Identify the Separate Performance Obligations in the Contract.
- Step 3: Determine the Transaction Price.
- Step 4: Allocating the Transaction Price to the Separate Performance Obligations in the Contract.
- Step 5: Recognize Revenue When (or as) the Entity Satisfies a Performance Obligation.

	ASC 985-605	Revised ED	Likely Impact[4]
		SCOPE	
Scope	This guidance generally applies to the following transactions and activities: • "Licensing, selling, leasing, or otherwise marketing computer software." • "The software and software-related elements of arrangements that include software that is more-than-incidental to the products or services in the arrangement as a whole." • "More-than-insignificant discounts on future purchases that are offered by a vendor in a software arrangement." • "Arrangements to deliver software or a software system, either alone or together with other products or services that require significant production, modification, or customization of software." (ASC 985-605-15-3) ASC 985-605 includes various scope exceptions, which are described in further detail in the sections below.	This guidance applies to all contracts with customers for the transfer of goods or services. Certain contracts, such as lease contracts, insurance contracts, guarantees, nonmonetary exchanges, and certain other contractual rights and obligations (i.e., most ASC financial instruments topics) are outside the scope of the revised ED. (9)[5] "A contract with a customer may be partially within the scope of [the revised ED] and partially within the scope of other [ASC topics]." If other topics specify how to separate or initially measure any parts of the contract, an entity first applies those separation or measurement requirements. If the other topics do not specify how to separate or initially measure any parts of the contract, the entity applies the revised ED to separate or initially measure those parts of the contract. (11)	Contracts previously accounted for under ASC 985-605 are within the scope of the revised ED. Entities will no longer have to evaluate whether an arrangement is within the scope of multiple revenue standards (e.g., ASC 985-605, ASC 605-35, and ASC 605-25). They will use a single, comprehensive model to account for all arrangements within the scope of the revised ED, and the prior guidance will be superseded.
Nonsoftware Deliverables in a Software Arrangement	ASC 985-605 does not provide guidance on separating nonsoftware-related deliverables that are within the scope of other literature from software and software-related deliverables. Therefore, entities generally first apply the separation and allocation guidance in ASC 605-25 to an arrangement that contains both software and nonsoftware deliverables.	The separation of a contract into separate performance obligations and the allocation of the transaction price are addressed by the revised ED. See Steps 2 and 4 of the five-step model, below.	Contracts previously accounted for under ASC 985-605 are within the scope of the revised ED. Entities will no longer have to evaluate whether an arrangement is within the scope of multiple revenue standards (e.g., ASC 985-605, ASC 605-35, and ASC 605-25). They will use a single, comprehensive model to account for all arrangements within the scope of the revised ED, and the prior guidance will be superseded.

[4] Likely impact is based on the revised ED as currently written and for typical contract terms. It is subject to interpretation and may not apply to all facts and circumstances.

[5] References are to paragraphs of the revised ED.

	ASC 985-605	Revised ED	Likely Impact
Software Components Excluded From the Scope of ASC 985-605	When an arrangement contains both nonsoftware components of tangible products and software components, the nonsoftware components are excluded from the scope of ASC 985-605. If it is determined that the software components and tangible products function together to deliver the tangible products' essential functionality, the essential software and any undelivered elements related to that essential software are excluded from the scope of ASC 985-605. (ASC 985-605-15-4)	All promised goods or services in a contract with a customer (e.g., software components, nonsoftware components, and tangible products) that do not meet any of the scope exceptions, are within the scope of the revised ED.	Contracts previously accounted for under ASC 985-605 are within the scope of the revised ED. Entities will no longer have to evaluate whether an arrangement is within the scope of multiple revenue standards (e.g., ASC 985-605, ASC 605-35, and ASC 605-25). They will use a single, comprehensive model to account for all arrangements within the scope of the revised ED, and the prior guidance will be superseded.
Arrangements Including Leased Software and Tangible Products	Under ASC 985-605, in arrangements involving a lease of software and hardware (e.g., property, plant, or equipment), revenue attributable to the hardware is accounted for in accordance with ASC 840, while revenue attributable to the software, including PCS, is accounted for in accordance with ASC 985-605 (provided that the software is more than incidental to the arrangement but not essential to the functionality of the combined product). If the software functions together with the leased equipment to deliver the product's essential functionality, the hardware, software, and software-related elements are outside the scope of ASC 985-605 and subject to other applicable accounting guidance (e.g., ASC 840, ASC 605-25, or SAB Topic 13).	A contract with a customer may be partially within the scope of the revised ED and partially within the scope of other ASC topics. If other topics specify how to separate or initially measure any parts of the contract, an entity first applies those separation or measurement requirements. If the other topics do not specify how to separate or initially measure any parts of the contract, the entity applies the revised ED to separate or initially measure those parts of the contract. (11) The FASB and IASB are also in the process of a complete overhaul of lease accounting. As currently proposed, the tentative lease guidance provides indicators for entities to use in determining whether an asset used by a supplier in the delivery of a service is separable from the arrangement as a whole (e.g., whether the asset is sold or leased separately by the supplier and whether the customer can use the asset on its own or together with other resources available to the customer). In situations in which a supplier directs how an asset is used to perform services for a customer, the customer and supplier must assess whether the use of the asset is separable from the services provided to the customer (e.g., computer and server equipment with outsourced information technology services or a cargo ship with time charter services). If the asset is separable, the arrangement could contain a lease if the asset is within the scope of the tentative lease accounting guidance (and thus is outside the scope of the proposed revenue guidance). However, if the use of an asset is an inseparable part of the services requested by the customer, the entire arrangement would be within the scope of the proposed revenue guidance.	Contracts previously accounted for under ASC 985-605 are within the scope of the revised ED. Entities will no longer have to evaluate whether an arrangement is within the scope of and comply with multiple revenue standards (e.g., ASC 985-605, ASC 605-35, and ASC 605-25). However, entities will still be required to separate and allocate contract consideration for goods and services that are within the scope of other standards.

	ASC 985-605	Revised ED	Likely Impact
Hosting Arrangements	A software element in a hosting arrangement is only within the scope of ASC 985-605 if the "customer has the contractual right to take possession of the software at any time during the hosting period without significant penalty [and it] is feasible for the customer to either run the software on its own hardware or contract with another party . . . to host the software." If the arrangement does not meet these two criteria, it would be accounted for as a service contract and would be outside the scope of ASC 985-605. (ASC 985-605-55-121)	Depending on the substance of a hosting arrangement, a customer may obtain control of the software itself, simply have the right to use it over time, or a combination of both. (See Step 4 below for a discussion of the factors that indicate whether control transfers over a period of time or at a point in time.) In other instances, the tangible products used to provide the hosting might be within the scope of the tentative lease accounting guidance (see Arrangements Including Leased Software and Tangible Products above).	Hosting arrangements, whether historically accounted for under ASC 985-605 or as a service contract, will be within the scope of the revised ED. Entities will have to closely evaluate the substance of the contract to determine whether the entity is (1) performing a service for which control is transferring over time or (2) in substance, licensing software for which control is transferred at a point in time and providing a separate hosting service (which may be the case when the criteria in ASC 985- 605-55-121 are met). While an entity will most likely consider factors similar to the scoping rules in ASC 985-605 to determine the substance of the arrangement and appropriate accounting in accordance with the revised ED, these criteria are not specifically included in the revised ED and thus not necessarily determinative of the accounting conclusion. Further, entities should closely evaluate the contractual terms of the hardware as it may meet the definition of a lease. If it does, the contract would need to be separated and initially measured as described in Arrangements Including Leased Software and Tangible Products above.
Software Requiring Significant Production, Modification, or Customization	Certain software sales involve significant production, modification, or customization of software. As stated in ASC 985-605-25-88, this arrangement is accounted for under ASC 605-35 by using the relevant guidance in ASC 985-605-25-88 through 25-107.	Contracts currently accounted for under ASC 605-35 are within the scope of the revised ED.	Contracts previously accounted for under ASC 985-605 or ASC 605-35 are within the scope of the revised ED. Entities will no longer have to evaluate whether an arrangement is in the scope of multiple revenue standards (e.g., ASC 985-605, ASC 605-35, and ASC 605-25). They will use a single, comprehensive model to account for all arrangements within the scope of the revised ED, and the prior guidance will be superseded.

<table>
<tr><th></th><th>ASC 985-605</th><th>Revised ED</th><th>Likely Impact</th></tr>
<tr><td colspan="4">STEP 1: IDENTIFY THE CONTRACT WITH A CUSTOMER</td></tr>
<tr><td>Persuasive Evidence of an Arrangement Exists</td><td>Practice varies with respect to the use of written contracts. Although a number of sectors of the industry rely upon signed contracts to document arrangements, other sectors of the industry that license software (notably the packaged software sector) do not.

If the vendor operates in a manner that does not rely on signed contracts to document the elements and obligations of an arrangement, the vendor should have other forms of evidence to document the transaction (e.g., a purchase order from a third party or online authorization). If the vendor's customary business practice is to use written contracts, evidence of the arrangement is provided only with a contract signed by both parties.</td><td>The revised ED defines a contract as an agreement between two or more parties that creates enforceable rights and obligations. Contracts can be written, oral, or implied by the entity's customary business practices. (13)

Under the proposed revenue requirements, a contract exists only if:
• "The contract has commercial substance."
• "The parties to the contract have approved the contract" and are committed to satisfying "their respective obligations."
• "The entity can identify each party's rights regarding the goods or services to be transferred."
• "The entity can identify the payment terms for the goods or services to be transferred." (14)

In addition, a contract does not exist if each party "has the unilateral enforceable right to terminate a wholly unperformed contract without compensating the other party (parties)." (15)</td><td>The definition of a contract under the proposed guidance differs from the definition of persuasive evidence of an arrangement under ASC 985-605. Depending on an entity's historical practice, these differences may result in accounting changes.

In addition, the requirement in ASC 985-605 that "collectibility is probable" for revenue to be recognized is not an explicit criterion in the revised ED. However, in the Basis for Conclusions of the revised ED, the boards indicated that a reasonable expectation of collectibility would be necessary for a contract to have commercial substance. Therefore, when an entity does not have a reasonable expectation of collectibility, a contract may not exist under the revised ED (and thus, revenue cannot be recognized). Some may interpret the current requirement (i.e., that collectibility is probable) as a different threshold than that in the revised ED (i.e., that the contract has commercial substance and therefore an entity has a reasonable expectation of collectibility).</td></tr>
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Combination of Contracts	"Software vendors may execute more than one contract or agreement with a single customer. However, a group of contracts or agreements may be so closely related that they are, in effect, parts of a single arrangement and should be viewed as one multiple-element arrangement [in the determination of] the appropriate amount of revenue to be recognized in accordance with [ASC 985-605]. The form of an arrangement is not necessarily the only indicator of the substance of an arrangement. The existence of any of the following factors (which are not all-inclusive) may indicate that a group of contracts should be accounted for as a single multiple-element arrangement:" • "[N]egotiated or executed within a short timeframe of each other." • Elements in contracts "are closely interrelated or interdependent in terms of design, technology, or function." • The fee for one "is subject to refund, forfeiture, or other concession if another contract is not [satisfied]." • One or more elements in one contract "are essential to the functionality" of another contract. • Payment terms in one contract "coincide with performance criteria of another contract." • Negotiated "jointly with two or more parties" to do a single project. (ASC 985-605-55-4)	An entity combines two or more contracts and accounts for them as a single contract if they are entered into at or near the same time with the same customer (or related parties) if one or more of the following criteria are met: • "The contracts are negotiated as a package with a single commercial objective." • "The amount of consideration . . . in one contract depends on the price or performance of the other contract." • The goods and services (or some goods or services) promised in the contracts meet the criteria to be accounted for as a single performance obligation. (17)	Other than the concept in the revised ED of potentially being required to combine contracts not only with the customer but also with parties related to the customer, the overall principles on combining contracts appear to be similar and are not likely to result in a significant change to current practice.

	ASC 985-605	Revised ED	Likely Impact
Modifications to a Software License and Side Agreements	Other than requiring the vendor to consider the implications of concessions, ASC 985-605 does not specifically discuss modifications to software arrangements. If a modification to a software arrangement is considered a concession, the vendor may need to evaluate whether the original fee was fixed or determinable and consider the impact on the accounting for future arrangements. Generally, previously recognized revenue is not affected and the vendor determines the impact of a modification prospectively on the basis of the facts and circumstances of the modification. Side agreements should be evaluated on a case-by-case basis to determine whether and how they affect the terms of the arrangement and thereby revenue recognition. A practice of entering into side agreements raises questions about what constitutes persuasive evidence of an arrangement and when, in fact, an arrangement has been consummated.	"A contract modification exists when the parties to a contract approve a change in the scope or price of a contract (or both)." (18) If the modification meets the contract criteria under the revised ED (discussed in Persuasive Evidence of an Arrangement Exists above), the accounting treatment depends on the nature of the modification. However, if the parties have approved a change in the scope but not the price, an entity would only account for the modification when the entity has an expectation that the price of the modification will be approved. A contract modification would be accounted for as a separate contract only if the modification results in (1) a separate performance obligation and (2) additional consideration that reflects the entity's stand-alone selling price of that separate performance obligation (when appropriate adjustments for the contract's particular circumstances are taken into account). Otherwise, an entity would evaluate the modified contract and allocate the remaining transaction price to the remaining performance obligations (prospectively) and update its measure of progress toward completion for performance obligations that are satisfied over time (which could result in a cumulative catch-up). However, if the modification to the contract is only a change in the transaction price, the modified transaction price would be reallocated to all performance obligations in the contract (see Step 4 below). (19–22, 78)	Although there is no explicit guidance, entities within the scope of ASC 985-605 generally account for contract modifications and side agreements prospectively. Since the revised ED specifically addresses accounting for contract modifications, it should improve discipline and consistency in accounting for contract modifications. The revised ED may result in a cumulative-effect adjustment when the modification is only to the transaction price (because the modified transaction price is reallocated to the separate performance obligations as if it existed at contract inception, potentially affecting the amount of revenue previously recognized for satisfied performance obligations). The revised ED does not specifically address side agreements, and entities will need to evaluate them on a case-by-case basis to determine whether they (1) represent terms in the original contract (and meet the contract criteria under the proposed guidance, discussed above) or (2) represent a contract modification (and should be accounted for under the contract modification guidance described above). If a side agreement represents terms that existed in the original contract and were not included in the original accounting for that contract, the entity should determine whether the adjustments for the impact of the side agreement result in an error under ASC 250.

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STEP 2: IDENTIFY THE SEPARATE PERFORMANCE OBLIGATIONS IN THE CONTRACT			
Multiple-Element Arrangements	Software arrangements commonly comprise multiple elements or deliverables (i.e., software and any combination of PCS, specified or unspecified software products or upgrades, additional licenses, services, or other nonsoftware deliverables). A vendor should separate a multiple-element arrangement to account for each component individually (in accordance with the specific guidance provided in ASC 985-605).	An entity identifies "which goods or services (or which bundles of goods or services) are distinct" and therefore accounted for as separate performance obligations. (23) The revised ED defines a performance obligation as "a promise in a contract with a customer to transfer a good or service to the customer." This obligation may be explicit in the contract or implied. (24) The revised ED lists what may be considered a good or service in a contract. (26). Entities evaluate the goods or services to determine the appropriate accounting units (i.e., separate performance obligations). See Separating the Arrangement below for additional discussion of how to determine the accounting units in a contract.	The promised goods or services in a contract are similar to the current concepts of a "deliverable" or "element." Once an entity determines the goods or services (explicit or implied) in the contract, it then must separate those goods or services into separate units of accounting. Because the revised ED is less restrictive in this area, many arrangements will have more units of accounting than under ASC 985-605. This could result in less deferral of revenue in situations in which VSOE of fair value does not exist for an undelivered element that could meet the separation criteria under the revised ED. This may require entities to closely evaluate the goods or services delivered earlier in an arrangement that may not have previously been given as much scrutiny because revenue was being deferred because of an undelivered element not having VSOE of fair value (e.g., PCS).
Separating the Arrangement	"If an arrangement includes multiple elements, the fee [is] allocated to the various elements [VSOE] of fair value, regardless of any separate prices stated in the contract for each element. [VSOE] of fair value is limited to the following:" • "The price charged when the same element is sold separately." • "For an element not yet being sold separately, the price established by management having the relevant authority; it must be probable that the price, once established, will not change before the separate introduction of the element into the marketplace." (ASC 985-605-25-6)	An entity accounts for a promise to transfer more than one good or service as a separate performance obligation if it is distinct. A good or service is "distinct" if the entity regularly sells it separately or the "customer can benefit from the good or service either on its own or together with other resources that are readily available." (27) Further, the boards decided that an entity would account for a bundle of goods or services as a single performance obligation if the goods or services are (1) "highly interrelated" and the entity provides "a significant service of integrating" them into a combined item or items and (2) significantly modified or customized to fulfill the contract. (28) "As a practical expedient, [when] two or more distinct goods or services . . . have the same pattern of transfer to the customer," an entity may combine them into one separate performance obligation. (30)	The revised ED replaces the specific rules under ASC 985-605 with a principle that is likely to increase the number of accounting units because of the less restrictive requirements in the revised ED to separate performance obligations. For example, the fact that VSOE of fair value does not exist for an undelivered element will not dictate whether goods or services in a contract can be separated. The "distinct" criteria provided in the revised ED are generally viewed as being consistent with the stand-alone value concept in ASC 605-25. Under the revised ED, an entity may need to use significant judgment when determining whether the goods or services are "highly interrelated" and "significantly modified or customized." The proposed ASU includes examples to illustrate this guidance; however, further clarification may be needed to ensure consistent application.

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Additional Products	As part of a bundled arrangement, a vendor may agree to "deliver specified additional software products in the future." Sometimes, a vendor offers the rights to these additional products as part of PCS. Generally, even when the additional products are included in PCS, the additional software product is a separate element in the contract. ASC 985-605 requires vendors to distinguish between specified and unspecified additional products. This determination is important because rights to specified products, including those offered on a when-and-if-available basis, must be treated as separate elements of the software arrangement. Conversely, the right to unspecified additional products is accounted for as a subscription. (ASC 985-605-25-47 through 25-59)	Specified and unspecified additional products may meet the criteria for treatment as separate performance obligations (see Separating the Arrangement above). In addition, if these extra products are provided as an option to the customer free of charge or at a discount, the option represents a separate performance obligation if it gives the customer a material right that it would not have received without entering into that contract. (IG20–IG24)	*Specified additional product* — The timing and measurement of revenue recognition may be accelerated under the revised ED. There is no longer a requirement to defer all revenue recognition unless or until VSOE of fair value is established for the specified additional product, or until all elements in the arrangement have been delivered. If an entity determines that a specified additional product meets the criteria to be accounted for as a separate performance obligation, the entity would allocate a portion of the consideration to that obligation on the basis of its relative stand-alone selling price (see Step 4 below) and recognize revenue upon transfer of control or the lapse of a right to future when-and-if-available products (see Step 5 below). *Unspecified additional product* — The revised ED may change the timing and measurement of revenue recognition (i.e., the bundle of all software-related revenue may be recognized in a pattern other than ratable over the term or economic life as a subscription). An entity would need to evaluate the facts and circumstances of the unspecified additional product and determine whether the unspecified additional products meet the criteria to be accounted for as a separate performance obligation.

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Upgrade Rights	ASC 985-605 requires vendors to distinguish between specified upgrades/enhancements and unspecified upgrades/enhancements. This determination is important because rights to specified upgrades/enhancements, including those offered on a when-and-if-available basis, must be treated as separate elements of the software arrangement to which revenue must be allocated. Conversely, rights to unspecified upgrades/ enhancements on a when-and-if-available basis are considered to be PCS. ASC 985-605 does not define "specified." However, an upgrade or product is generally considered to be "specified" if it is described in enough detail for both the vendor and the customer to determine whether the vendor's obligation to deliver the upgrade or product has been extinguished. The description can range from a detailed report on the upgrade or product's features and functionality (such as a product "roadmap") to a mere statement of its name or version number. Finally, no discount in a bundled arrangement is allocable to specified upgrade rights. (ASC 985-605-25-44 through 25-46)	Specified and unspecified upgrade rights represent goods or services in the contract that would be analyzed to determine whether they meet the criteria to be treated as separate performance obligations (see Separating the Arrangement above). In addition, if these upgrade rights are provided as an option to the customer free of charge or at a discount, the option represents a separate performance obligation if it provides the customer a material right that it would not have received without entering into that contract. (IG20–IG24)	*Specified upgrade right* — While there may be exceptions due to individual facts and circumstances, a specified upgrade right would generally meet the separation criteria because the customer would be likely to receive benefit from the upgrade with other resources readily available to the customer (i.e., the software obtained in the prior purchase). The revised ED does not contain a rule that a discount is not able to be allocated to a specified upgrade right. (See Step 4 below for additional discussion of allocating the transaction price.) Control would generally transfer at the point in time that the customer receives the specified upgrade. (See Step 5 below for additional discussion of when control transfers to the customer.) *Unspecified upgrade right* — Unspecified upgrades are likely to be accounted for as they are under current practice. Generally, customers pay a periodic fee for the right to unspecified when-and-if-available upgrades and would most likely meet the criteria that control transfers over time. (See Step 5 below.)

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Postcontract Customer Support	PCS revenue is generally recognized in the same pattern (i.e., ratably over the PCS period) regardless of whether it is sold separately or as part of an overall arrangement. If historical evidence suggests that costs to provide PCS are incurred on other than a straight-line basis, then revenue should be recognized in proportion to the amounts expected to be charged to expense for the PCS services. Because PCS is generally not considered essential to the functionality of other deliverables in an arrangement, it is usually viewed as a separate element. As with other software elements, a portion of the arrangement fee must be allocated to PCS on the basis of VSOE of fair value (and recognized over the PCS period in accordance with ASC 985-605). If VSOE of fair value cannot be established and the PCS is the only remaining undelivered element, the entire arrangement fee must be recognized ratably over the stated PCS period (if explicitly stated in the contract) or the period over which PCS services are expected to be provided (if implicit rights to PCS exist). VSOE of fair value for PCS is generally evidenced by the price the customer will be required to pay when it is sold separately (i.e., the renewal rate).	PCS would generally be accounted for as a separate performance obligation. It would most likely be distinct from the other goods or services in the contract since it is either sold separately (as evidenced through subsequent renewals) or the customer can benefit from the software without the PCS. See Recognition of PCS Revenue Upon Delivery of the Related Software in Step 5 below for additional discussion of the revised ED for revenue recognition for PCS.	Because the revised ED is less restrictive in separating and allocating contract consideration, there are likely to be fewer instances in which all revenue is required to be deferred for a bundle of goods or services to be recognized ratably over the PCS period. See Recognition of PCS Revenue Upon Delivery of the Related Software in Step 5 below for additional discussion of likely impact to revenue recognition for PCS.
Warranty-Related Services	Warranties that protect customers from defective software and that are routine, short-term, and relatively minor, are not considered PCS and should be accounted for in accordance with ASC 450. (ASC 985-605-25-37) However, PCS may include certain warranty-type services such as the correction of errors (e.g., bug fixes). (ASC 985-605-55-77)	"If a customer has the option to purchase a warranty separately" from the entity, the entity should account for the "warranty as a separate performance obligation because the entity [is providing a service] in addition to the product." Therefore, the entity would allocate revenue to the warranty service. (IG11) "If a customer does not have the option to purchase a warranty separately [from the entity,] the entity should account for the warranty in accordance with [ASC 460-10]" (cost accrual model) unless the warranty provides a service to the customer "in addition to the assurance that the product complies with [the contract's] agreed-upon specifications" (in which case the entity would account for the warranty service as a separate performance obligation). (IG12 and IG14)	The revised ED for separately priced warranty options or warranties beyond assuring an entity's past performance may result in the allocation and deferral of contract consideration in certain circumstances rather than accrual of costs (as may be the case under current GAAP). Most likely this will have a limited impact on typical software arrangements since a separately priced warranty under existing guidance is often viewed as PCS.

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Postdelivery Telephone Support	ASC 985-605 requires that postdelivery telephone support that is offered or available to customers at no additional charge be accounted for as PCS. Generally, the arrangement consideration allocated to the telephone support would have to be recognized as revenue over the period during which the telephone support is expected to be provided unless the ASC 985-605-25-71 conditions are met, in which case the revenue allocable to telephone support may be recognized together with the initial licensing fee on delivery of the software (substantially all telephone support services are performed within one year of the date of software delivery).	Postdelivery telephone support is most likely a service in the contract and an entity must evaluate if the service represents a separate performance obligation. If it does not meet the separation criteria, the service should be combined with another good or service until that bundle is distinct. (27)	The revised ED does not explicitly include the exceptions that would allow for postdelivery telephone support to be recognized upon delivery of the software license. Rather, an entity would have to conclude that the services to be provided are not material in accordance with ASC 105 to conclude that these services do not require allocation and deferral of a portion of the consideration in the arrangement. ASC 105 states that the guidance in the ASC does not need to be applied to immaterial items. (BC66)
Indemnification Clauses	The standard software license agreement of a software vendor often includes a clause that provides for indemnification for liabilities and damages arising from any claims of patent, copyright, trademark, or trade secret infringement by the software vendor's software. This type of indemnification is not an element that can be separated from the software; rather, it is an inherent component of the software license itself and is similar to a standard warranty.	"[A]n entity's promise to indemnify the customer for liabilities and damages arising from claims of patent, copyright, trademark, or other infringement by the entity's products does not give rise to a performance obligation." The entity accounts for such obligations in accordance with the guidance on loss contingencies in ASC 450-20. (IG15)	It is not likely that this will have a significant impact because the provisions of the revised ED are consistent with current practice.

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STEP 3: DETERMINE THE TRANSACTION PRICE			
Vendor's Fee Is Fixed or Determinable — Extended Payment Terms	Under ASC 985-605, an arrangement fee must be fixed or determinable before revenue can be recognized. If a vendor cannot conclude that the fee is fixed or determinable at the outset of an arrangement, revenue would be recognized as payments from the customer become due (provided that all other requirements for revenue recognition are met). In arrangements with extended payment terms, it may be less likely that the vendor will collect the full payment stipulated in the payment terms and the arrangement fee may not meet the fixed-or-determinable criterion. ASC 985-605-25-34 specifies that an arrangement fee is presumed not to be fixed or determinable "if payment of a significant portion of the software licensing fee is not due until after expiration of the license or more than 12 months after delivery."	An entity's objective when determining the transaction price is to estimate the total amount of consideration to which the entity expects to be entitled under the contract. To meet that objective, an entity should use either of the following methods to estimate the transaction price, depending on which method better predicts the amount of consideration to which the entity will be entitled: • The expected value (i.e., probability-weighted amount). • The single most likely amount. (55) An entity should adjust the promised amount of consideration to reflect the time value of money if the contract includes a significant financing component. The revised ED contains factors for entities to consider in determining whether the effect of financing is significant to the contract. As a practical expedient, an entity should not assess whether a contract has a significant financing component if the "period between payment by the customer [and] the transfer of the promised goods or services to the customer [is] one year or less." (58–62)	The revised ED may represent a significant change from current practice for extended payment terms. That is, extended payment terms may (1) be indicators of a significant financing component to the contract, (2) affect the calculation of the expected value or most likely amount, or (3) change the uncertainty regarding collectibility (discussed in the next section). This step in the proposed model simply calculates the amount of revenue that is expected to be received from the contract. While much of the guidance in the subheadings under this step may affect the transaction price calculation, the topics in these subheadings may also affect the amount that the entity is reasonably assured to be entitled to in the determination of the amount of revenue to be recognized (see Step 5 below).
Vendor's Fee Is Fixed or Determinable and Collectability Is Probable	Under ASC 985-605, the evaluation of collectibility focuses both on whether the customer has the intent and ability to pay (i.e., creditworthiness) and on whether the fee is deemed fixed or determinable.	The revised ED does not include a specific recognition threshold requiring that collectibility be probable. Rather, implicit in the "commercial substance" criterion for when a contract exists is a notion that requires a reasonable expectation of collectability. (BC168–BC170) Initial and subsequent adjustments for collectibility (i.e., a customer's credit risk or bad-debt expense) are shown as a reduction of revenue in a separate line item (i.e., contra revenue below gross revenue) and are measured in accordance with ASC 310 (69).	Some could interpret the thresholds of "collectibility is probable" and "reasonable expectation of collectibility" as being different. In certain circumstances, this difference could affect the timing and measurement of revenue recognition. The presentation of collectibility adjustments in a separate line item is a change from the current presentation requirements. See additional discussion in Persuasive Evidence of an Arrangement Exists above.

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Price-Protection Clauses	If a vendor offers a customer a price-protection clause and cannot reasonably estimate future price changes, or if the vendor's ability to maintain its price is uncertain, the fee would not be fixed and determinable and revenue should be deferred until the vendor's liability under the price-protection clause can be reasonably estimated (provided that all other requirements for revenue recognition are met).	An entity's objective when determining the transaction price is to estimate the total amount of consideration to which the entity expects to be entitled under the contract. To meet that objective, an entity should use either of the following methods to estimate the transaction price, depending on which method better predicts the amount of consideration to which the entity will be entitled: • The expected value (i.e., probability-weighted amount). • The single most likely amount. (55) An entity must recognize revenue from satisfying a performance obligation in the amount to which the entity is reasonably assured to be entitled. (81) (See Step 5 below for additional discussion of constraining recognized revenue to the amount that is reasonably assured.)	Future price changes would be included in the entity's estimate of the transaction price. This estimate would be updated in each reporting period and would affect the amount of revenue recognized. However, the cumulative amount recognized would be limited to the amount that is reasonably assured (see Step 5 below for additional discussion). Unlike current practice, which could require deferral of the entire amount, the revised ED may only require deferral for a lesser amount (i.e., the amount that is not reasonably assured).
Customer Cancellation Privileges and Forfeiture or Refund Clauses	Arrangements with customer cancellation privileges do not meet the fixed or determinable fee recognition criteria until the cancellation privileges lapse. When the cancellation privileges expire ratably over the license period, the fees become determinable and revenue is recognized ratably over the license period as the privileges lapse. (ASC 985-605-25-37) No portion of the fee (including amounts otherwise allocated to delivered elements) meets the collectibility criterion if the portion of the fee allocable to delivered elements is subject to forfeiture, refund, or other concession if any of the undelivered elements are not delivered.	Customer cancellation privileges and forfeiture or refund clauses are accounted for as a right of return. When a right of return exists, an entity recognizes (1) revenue for goods or services that have been transferred to the customer and whose return is not reasonably assured, (2) a refund liability, and (3) (if applicable) an asset (including an adjustment to cost of sales) for the right to recover returned goods. If an entity is not reasonably assured of the amount that will be refunded, revenue should not be recognized until such an amount is reasonably assured (which may not be until the right of return expires). (IG2–IG9)	Under the revised ED, when an entity is reasonably assured to be entitled to consideration before the expiration of the cancellation, forfeiture, or refund period, revenue may be recognized earlier than it is under current practice. That is, revenue from contracts that an entity does not expect to be canceled may be recognized when the performance obligations are satisfied.

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Fiscal Funding Clauses	A fiscal funding clause with a customer other than a governmental unit that is required to include such a clause creates a contingency that precludes revenue recognition until the requirements of the clause and all other provisions have been satisfied.	An entity's objective when determining the transaction price is to estimate the total amount of consideration to which the entity expects to be entitled under the contract. To meet that objective, an entity should use either of the following methods to estimate the transaction price, depending on which method better predicts the amount of consideration to which the entity will be entitled: • The expected value (i.e., probability-weighted amount). • The single most likely amount. (55) An entity must recognize revenue from satisfying a performance obligation in the amount to which the entity is reasonably assured to be entitled. (81) (See Step 5 below for additional discussion of constraining recognized revenue to the amount that is reasonably assured.)	Under the revised ED, when an entity is reasonably assured to be entitled to consideration before the resolution of the contingency created by the fiscal funding clause, revenue may be recognized earlier than it is under current practice. That is, revenue in the amount that an entity is reasonably assured will not be canceled by the customer as a result of the fiscal funding clause may be recognized when the performance obligations are satisfied. Determining the amount that is reasonably assured in accordance with the revised ED may require significant judgment.
Discounts	A vendor may offer a customer a right to a pricing discount on a future purchase of a product or service. If this discount is more than insignificant, the right to it is considered an element in the arrangement. (ASC 985-605-15-3(d))	The "option to acquire additional goods or services at a discount [represents a] performance obligation [if it] provides a material right to the customer" that would not otherwise have been received. (IG20 and IG21) "If a customer has the option to acquire an additional good or service at a price" that is within the range of prices typically charged for those goods or services, "that option does not provide the customer with a material right even if the option can be exercised only because [a] previous contract" was entered into. The "entity has merely made a marketing offer." (IG22)	The guidance in ASC 985-605 and the revised ED appear similar; thus, it is not likely that the proposed provision will have a significant impact.

	ASC 985-605	Revised ED	Likely Impact
Fixed-Fee Arrangements Based on a Price per Copy	When a fixed-fee arrangement does not specify the maximum number of copies allowed, the allocation of the arrangement fee to the products is not possible because it depends on the number of copies ultimately made of each product. Revenue is recognized as copies are delivered. However, all unrecognized revenue in the arrangement is recognized when the vendor is not obligated to deliver additional products and either (1) delivery of all products is complete or (2) total revenue resulting from the copies produced equals the arrangement's fixed fee.	If "an entity grants a customer the option to acquire additional goods or services, that option gives rise to a separate performance obligation in the contract only if the option provides a material right to the customer that it would not receive without entering into that contract. . . . If the option provides a material right, . . . the customer in effect pays the entity in advance for future goods or services and the entity recognizes revenue when those future goods or services are transferred or when the option expires." (IG20 and IG21) Regardless of whether the arrangement specifies the maximum number of copies allowed, the entity would allocate the fixed consideration among the separate performance obligations (i.e., expected number of copies to be transferred to the customer over the life of the arrangement) and would recognize revenue when each copy is transferred in a manner that best depicts the transfer of control. However, the entity would need to reevaluate its performance in relation to the number of copies expected to be delivered when it is measuring its performance to date in each period.	The right to reproduce or obtain copies of software products at a specified price per copy would be considered a customer option for additional goods or services. If the right/option to reproduce or obtain copies of software products would provide the customer with a material right that the customer would not receive without entering into the arrangement, each additional copy of the software would be considered a separate performance obligation. Regardless of whether the arrangement specifies the maximum number of copies allowed, the entity would allocate the fixed fee or transaction price among the separate performance obligations (i.e., expected number of copies to be transferred to the customer over the life of the contract) and would recognize revenue when control for each performance obligation is transferred.
Platform-Transfer Rights	For end users, depending on the terms of the arrangement, platform-transfer rights should be classified as a return, as an exchange (if it is for the same product and does not increase the number of copies or concurrent users under the license agreement), or as an additional software product (if the terms allow the customer to continue using a previously delivered software product in addition to the software related to the new platform).	There are no specific requirements for platform-transfer rights. An entity should closely evaluate the terms of the contract and should determine whether the transfer rights represent a return, an exchange, or an additional software product. See Rights to Exchange or Return Software Products in Step 5 below and Additional Software Product in Step 2 above for guidance on each type of contract.	See discussion in Step 5 on "Rights to Exchange or Return Software Products" and Step 2 on "Additional Software Product" for guidance on each type of contract.

	ASC 985-605	Revised ED	Likely Impact
STEP 4: ALLOCATE THE TRANSACTION PRICE TO THE SEPARATE PERFORMANCE OBLIGATIONS IN THE CONTRACT			
Allocating Consideration	The allocation of the consideration to elements in a multiple-element software arrangement and the subsequent recognition of such consideration depend on whether VSOE of fair value has been established. If VSOE of fair value is established for all undelivered elements, the portion of the fee allocated to an element (on the basis of VSOE of fair value) should be recognized as revenue when the recognition criteria are met for each element (unless an undelivered element in an arrangement is considered essential to the functionality of a delivered element). If VSOE of fair value is not established, all revenue from the arrangement must be deferred until the earlier of (1) the establishment of VSOE of fair value or (2) the delivery of all elements in the arrangement (with certain exceptions, as listed in ASC 985-605-25-10). The exceptions in ASC 985-605-25-10 include the use of a residual method.	The transaction price is allocated on a relative stand-alone selling price basis (stand-alone selling price should be estimated if it is not observable). Suitable estimation methods include expected cost plus margin, adjusted market assessment, and the residual approach (in certain limited circumstances). The residual approach does not specifically preclude the use of a reverse residual allocation (i.e., use of a residual method to estimate the stand-alone selling price for an undelivered item). (70–73) When specific conditions are met, certain discounts or amounts that are contingent on a future event may be allocated to one or more specific separate performance obligations. (74–76) After contract inception, changes in the transaction price are generally allocated to all performance obligations (on the basis of initial allocation). However, subsequent changes in the transaction price that are related to a contingent future event may be allocated to one or more specific performance obligations (when certain conditions are met). (77–80)	An entity may be less constrained by the revised ED's allocation requirements for revenue recognition than it is under the current requirements. The revised ED allows entities to use estimates, in the absence of observable prices, to determine the stand-alone selling price. Although the revised ED includes three examples of suitable estimation methods, it does not prescribe one. Therefore, an entity would be allowed some judgment in determining a method of estimation as long as it maximizes the use of observable inputs and is applied consistently to goods or services and customers with similar characteristics. As a result, and because of an entity's ability to use a reverse residual method, revenue may be allocated differently under the revised ED than it is under ASC 985-605 in certain circumstances. Entities that currently find it difficult to obtain VSOE of fair value will be given significantly more judgment to use estimates to demonstrate stand-alone selling prices, increasing the likelihood that revenue will be recognized when each performance obligation is satisfied.

	ASC 985-605	Revised ED	Likely Impact
STEP 5: RECOGNIZE REVENUE WHEN (OR AS) THE ENTITY SATISFIES A PERFORMANCE OBLIGATION			

Delivery Has Occurred	The second criterion in ASC 985-605-25-3 for revenue recognition is delivery. The principle of not recognizing revenue before delivery applies regardless of whether the customer is a *user* or *reseller*. Except for arrangements in which the fee is a function of the number of copies, delivery is considered to have occurred upon the transfer of the *product master* or, if the product master is not to be delivered, upon the transfer of the first copy. For software that is delivered electronically, the delivery criterion in that paragraph is considered to have been met when either of the following has occurred:
	• The customer has taken possession of the software via a download (i.e., when the customer takes possession of the electronic data on its hardware).
	• The customer has been provided with access codes that allow the customer to take immediate possession of the software on its hardware pursuant to an agreement or purchase order for the software.
		An entity satisfies a performance obligation when control of the good or service underlying the obligation has been transferred to the customer. Control of a good or service can be transferred to a customer, and hence an entity can satisfy a performance obligation, at a point in time or over time.
		An entity satisfies a performance obligation over time if either of the following occurs:
		• "The entity's performance creates or enhances an asset . . . that the customer controls as the asset is created or enhanced."
		• "The entity's performance does not create an asset with an alternative use to the entity" and at least one of the following is met:
		    ◦ "The customer simultaneously receives and consumes the benefits of the entity's performance as [it] performs."
		    ◦ "Another entity would not need to substantially reperform the work [performed] to date if that other entity were to fulfill the remaining obligation to the customer."
		    ◦ "The entity has a right to payment for performance completed to date and [is expected] to fulfill the contract." (35)
		Revenue is recognized for separate performance obligations that are satisfied over time by measuring the entity's "progress toward complete satisfaction of [the] performance obligation" in a manner that best depicts the transfer of goods or services to the customer. (38–40) The proposed ASU provides specific guidance on the use and application of an output method and an input method for measuring progress toward completion. (41–46) The amount recognized is limited to the amount to which the entity is reasonably assured to be entitled. (81)
			The criteria for when a customer obtains control of a good or service at a point in time are generally consistent with the types of items considered in the assessment of whether and when delivery has occurred.
			Under the proposed model, services will generally be unbundled and recognized over time as the service obligations are satisfied (assuming that the separation criteria in Step 2 are met).
			See additional discussion below for guidance on accounting for a good or service satisfied over time.

	ASC 985-605	Revised ED	Likely Impact
Delivery Has Occurred (continued)		If a performance obligation does not meet the criteria for satisfaction over time, it is satisfied at a point in time. The proposed ASU states that indicators that control of an asset has been transferred to a customer at a point in time include, but are not limited to, the following: • "The entity has a present right to payment." • "The customer has legal title." • "The entity has transferred physical possession." • "The customer has the significant risks and rewards of ownership." • "The customer has accepted the asset." (37)	
Customer Acceptance	Software arrangements often include specific customer acceptance provisions; ASC 985-605 indicates that if the customer's acceptance of the software is uncertain, revenue should not be recognized until acceptance occurs. Further, if payment for the software is tied to customer acceptance, the acceptance provision would be presumed substantive. Therefore, provided that all other requirements for revenue recognition have been met, revenue recognition would be precluded until payment is made or due unless that presumption is overcome.	Customer acceptance is one of the indicators that an entity must consider in determining the point in time at which control is transferred for a good or service provided to a customer. (37e) The effect of the acceptance clauses on determining whether a customer has obtained control of a promised good or service depends on whether an entity can objectively determine that a good or service has been transferred to the customer in accordance with the agreed-upon specifications in the contract. "If an entity can objectively determine that control of a good or service has been transferred to the customer in accordance with the agreed-upon specifications," the customer acceptance provisions would not affect the determination of control transfer. If an entity cannot objectively make this determination, it would not be able to conclude that it has obtained control until it receives the customer's acceptance. (IG55–IG58)	It is not likely that these provisions of the revised ED will have a significant impact since they are consistent with current practice. However, the revised ED does not include a presumption that the customer's acceptance provisions are substantive if they are tied to payment, which could affect the timing of revenue recognition.

	ASC 985-605	Revised ED	Likely Impact
Keys or Authorization Codes	In software arrangements involving the use of keys, a vendor is not necessarily required to deliver a key to fulfill its delivery responsibility. The software vendor recognizes revenue on delivery of the software if all of the following conditions are met (provided that all other requirements for revenue recognition in ASC 985-605 are met): • "The customer has licensed the software and the vendor has delivered a version of the software that is fully functional except for the permanent key or the additional keys (if additional keys are used to control the reproduction of the software)." • "The customer's obligation to pay for the software and the terms of payment, including the timing of payment, are not contingent on delivery of the permanent key or additional keys (if additional keys are used to control the reproduction of the software)." • "The vendor will enforce and does not have a history of failing to enforce its right to collect payment under the terms of the original arrangement." (ASC 985-605-25-28)	A customer obtains control of a good or service when the customer has the ability to direct the use of, and receive the benefit from, the good or service. When a performance obligation does not meet the criteria to be satisfied over time, it is satisfied at a point in time. The proposed ASU states that indicators that control of an asset has been transferred to a customer at a point in time include, but are not limited to, the following: • "The entity has a present right to payment." • "The customer has legal title." • "The entity has transferred physical possession." • "The customer has the significant risks and rewards of ownership." • "The customer has accepted the asset." (37)	In these circumstances, an entity needs to evaluate whether the customer has the ability to direct the use of, and receive benefit from, the good or service under the proposed standard. If the software does not function without the keys or codes, the treatment would be similar. An entity will also need to evaluate the specific facts and circumstances associated with the use of keys and how they affect the evaluation of whether the customer has obtained control of the good or service. For example, if the key is used solely to protect against the customer's failure to comply with the terms of the contract, control may still have been transferred; however, if the key is used to control the use for a trial period or for demonstration purposes, then control may not have been transferred to the customer.

	ASC 985-605	Revised ED	Likely Impact
Reseller Arrangement Terms	For reseller arrangements, if any of the following factors or conditions exist, they are also considered in the evaluation of whether the revenue recognition criteria for fixed or determinable fee and collectibility are met: • Business practices, the reseller's operating history, competitive pressures, informal communications, or other factors indicate that payment is substantially contingent on the reseller's success in distributing individual units of the product. Contractual arrangements under which the reseller is obligated to pay only as and if sales are made to users are accounted for as consignments. • Resellers are new, undercapitalized, or in financial difficulty and may not demonstrate an ability to honor a commitment to make fixed or determinable payments until they collect cash from their customers. • Uncertainties about the potential number of copies to be sold by the reseller may indicate that the amount of future returns cannot be reasonably estimated on delivery. Examples of such factors include the newness of the product or marketing channel, competitive products, or dependence on the market potential of another product offered (or anticipated to be offered) by the reseller. • Distribution arrangements with resellers require the vendor to rebate or credit a portion of the original fee if the vendor subsequently reduces its price for a product and the reseller still has rights with respect to that product (sometimes referred to as price protection). If a vendor is unable to reasonably estimate future price changes in light of competitive conditions, or if there is significant uncertainty regarding the vendor's ability to maintain its price, the arrangement fee is not fixed or determinable. In such circumstances, revenue from the arrangement is deferred until the vendor is able to reasonably estimate the effects of future price changes and the other conditions have been satisfied.	"When an entity delivers a product to another party (such as a dealer or a distributor) for sale to end customers, the entity [evaluates] whether [the dealer or distributor] has obtained control of the product at that point in time" in accordance with paragraph 37. (IG49) "Inventory on consignment typically is controlled by the entity until a specified event occurs, such as the sale of the product to a customer of the dealer, or until a specified period expires. Until that point, the entity typically is able to require the return of the products or to transfer them to another dealer. Moreover, the dealer typically does not have an unconditional obligation to pay for the products (although it might be required to pay a deposit). Accordingly, in those circumstances, the entity would not recognize revenue upon delivery of the products to the dealer." (IG50)	The factors in ASC 985-605-25-36 concern specific terms of the contract that would preclude an entity from being able to assert that its fee is fixed or determinable and collectibility is probable and that it thus would prevent revenue recognition. Under the revised ED, many of these factors and conditions would not affect the timing or revenue recognition but would instead affect the determination of the transaction price (e.g., price protection clauses, extended payment terms) or collectibility adjustments (reseller's ability to pay). As a result of these differences, the timing and measurement of revenue recognition under the revised ED may be different from current practice.

	ASC 985-605	Revised ED	Likely Impact
Rights to Exchange or Return Software Products	*Right of exchange* — A customer's right to exchange is the right to replace a software product for another software product that has no more-than-minimal differences in price, functionality, or features. For the transaction to be accounted for as an exchange, the customer should not have the right to continue using the original product. In accounting for a right of exchange, a vendor does not reduce revenue for expected customer exchanges; however, the estimated costs of executing such exchanges should be accrued in accordance with ASC 450-20. *Right of return* — A customer's right to return is the right to return a software product for a refund (or to exchange a software product for another product that has more-than-minimal differences in price, functionality, or features). In accounting for a right of return, a vendor must be able to reasonably estimate expected product returns when recognizing revenue. In a manner consistent with ASC 605-15-25-1 through 25-4, revenue recognized should be reduced to reflect the estimated returns and the estimated costs of executing such returns should be accrued in accordance with ASC 450. If the vendor is unable to reasonably estimate returns, revenue must be deferred until a reasonable estimate can be made or the right of return has lapsed.	*Right of exchange* — "Exchanges by customers of one product for another of the same type, quality, condition, and price (for example, one color or size for another) are not considered returns" under the proposed requirements. (IG8) *Right of return* — An entity recognizes the following for transferred products with a right of return: • Revenue for products transferred that the entity is reasonably assured will not be returned. • A refund liability (amount of consideration expected to be refunded). • An asset (and equal adjustment to cost of sales) for the entity's right to recover the transferred goods upon settling the refund liability. (IG3) If an entity is not reasonably assured of the quantity of goods to be returned, the entity must recognize any consideration received as a refund liability (and should not recognize revenue). In such cases, the entity recognizes revenue when it determines that it is reasonably assured of the quantity of goods that will not be returned. (IG7) An entity updates the "measurement of the refund liability at the end of each reporting period for changes." (IG6)	The guidance in ASC 985-605 and the proposed guidance appear to be similar; thus, it is not likely that this provision will have a significant impact.

	ASC 985-605	Revised ED	Likely Impact

Recognition of PCS Revenue Upon Delivery of the Related Software	PCS revenue may be recognized upon delivery of the related software product if the following criteria are met:
	• The PCS fee "is included with the initial licensing fee."
	• The PCS is included with the initial licensing fee "for one year or less."
	• The "estimated cost of providing [PCS] during the arrangement is insignificant."
	• "Unspecified upgrades or enhancements offered during [the PCS arrangement] historically have been and are expected to be . . . minimal and infrequent." (ASC 985-605-25-71)
		Revenue should be recognized for each separate performance obligation upon transfer to the customer (which may occur at a point in time or over a period of time). Typically, PCS transfers to the customer over time (i.e., over a stated PCS period).
		An entity satisfies a performance obligation over time if either of the following occurs:
		• "The entity's performance creates or enhances an asset . . . that the customer controls as the asset is created or enhanced."
		• "The entity's performance does not create an asset with an alternative use to the entity" and at least one of the following criteria is met:
		    ○ "The customer simultaneously receives and consumes the benefits of the entity's performance as [it] performs."
		    ○ "Another entity would not need to substantially reperform the work [performed] to date if that other entity were to fulfill the remaining obligation to the customer."
		    ○ "The entity has a right to payment for performance completed to date and [is expected] to fulfill the contract." (35)
		Revenue is recognized for separate performance obligations that are satisfied over time by measuring the entity's "progress toward complete satisfaction of [the] performance obligation" in a manner that best depicts the transfer of goods or services to the customer. (38–40) The proposed ASU provides specific guidance on the use and application of an output method and an input method for measuring progress toward completion. (41–46) The amount recognized is limited to the amount to which the entity is reasonably assured to be entitled. (81)
		Revenue is allocated to each separate performance obligation on the basis of its relative stand-alone selling price. For PCS, the stand-alone selling price would generally be established by (1) separate sales or (2) substantive renewal rates.
			The revised ED does not include an exception that allows PCS revenue recognition upon delivery of the related software. Some entities may reach the same accounting conclusion when they determine that the PCS fee is not material in accordance with ASC 105 (which states that the guidance in the ASC does not need to be applied to immaterial items). However, an entity may determine that a change to current accounting is warranted on the basis of its evaluation of the threshold in ASC 985-605 regarding the terms "insignificant" and "immaterial" in ASC 105.

	ASC 985-605	Revised ED	Likely Impact
Delayed Start for PCS	The PCS term of a software arrangement may not begin as of the delivery date of the software (e.g., PCS may begin after installation or the expiration of a warranty period). In such situations, (1) the PCS agreement typically allows the customer to receive any upgrades or enhancements released by the vendor in the period between delivery of the license and the beginning of the PCS term, and (2) there is an implied PCS arrangement that begins upon delivery of the software. A portion of the fee should be allocated to the implied PCS arrangement on the basis of VSOE of fair value for the elements in the arrangement. VSOE of fair value for the implied PCS may be derived on a pro rata basis from the VSOE of fair value of the contractual PCS arrangement, particularly PCS renewal rates.	Goods or services in a contract do not need to be explicitly stated; they may be implied on the basis of an entity's customary business practices. (24) If a customer is able to receive upgrades or enhancements released by the entity in the period between delivery of the license and the beginning of the contractual PCS term, an implied PCS service obligation most likely exists. An entity should determine whether the PCS meets the criteria for a separate performance obligation and, if so, allocate revenue to it on the basis of its relative stand-alone selling price. Revenue should be recognized by using the method that best depicts the transfer of the PCS to the customer (to the extent that it is reasonably assured).	Unlike ASC 985-605, the proposal does not contain prescriptive guidance; however, the principles in the revised ED would most likely result in similar accounting, so it is not likely that the new provisions will have a significant impact.
Services	Certain arrangements include both software and service elements (other than PCS-related services). The services may include training, installation, or consulting. Consulting services often include implementation support, software design or development, or the customization or modification of the licensed software. If an arrangement includes such services, an entity determines whether the service element can be accounted for separately as the services are performed. ASC 985-605-25-78 discusses the criteria that an entity must consider in making such a determination. If the nature of the services is such that the service element does not qualify for separate accounting as a service, the entity applies contract accounting to both the software and service elements of the arrangement. ASC 985-605-25-88 through 25-107 address the application of contract accounting to software arrangements.	Revenue should be recognized for each separate performance obligation upon transfer to the customer (which may occur at a point in time or over a period of time). An entity satisfies a performance obligation over time if either of the following occurs: • "The entity's performance creates or enhances an asset . . . that the customer controls as the asset is created or enhanced." • "The entity's performance does not create an asset with an alternative use to the entity" and at least one of the following criteria is met: ◦ "The customer simultaneously receives and consumes the benefits of the entity's performance as [it] performs." ◦ "Another entity would not need to substantially reperform the work [performed] to date if that other entity were to fulfill the remaining obligation to the customer." ◦ "The entity has a right to payment for performance completed to date and [is expected] to fulfill the contract." (35)	The revised ED is less restrictive than current guidance because it removes the requirement that VSOE of fair value must exist before a good or service in a multiple-element contract may be treated as a separate unit of accounting. Under the revised ED, services that previously were bundled may qualify for separation and be recognized as the service obligations are satisfied. The revised ED will likely increase the number of accounting units.

	ASC 985-605	Revised ED	Likely Impact
Services (continued)	• The services are not essential to the functionality of any other element of the transaction. • The services are described in the contract such that the total price of the arrangement would be expected to vary as the result of the inclusion or exclusion of the services. If an arrangement includes services that meet the criteria of ASC 985-605-25-78 for separate accounting, revenue is allocated among the service and software elements of the contract. This allocation should be based on VSOE of fair values. (Fair values are not necessarily the same as any separate prices stated for the separate elements of the arrangement.) Revenue allocated to the service element is recognized as the services are performed or, if no pattern of performance is discernible, on a straight-line basis over the period during which the services are performed.	Revenue is recognized for separate performance obligations that are satisfied over time by measuring the entity's "progress toward complete satisfaction of [the] performance obligation" in a manner that best depicts the transfer of goods or services to the customer. (38–40) The proposed ASU provides specific guidance on the use and application of an output method and an input method for measuring progress toward completion. (41–46) The amount recognized is limited to the amount to which the entity is reasonably assured to be entitled. (81)	

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