Working Draft:
Software Revenue Recognition Implementation Issue

Issue #14-8: Transfer of Control for Distinct Software Licenses

Expected Overall Level of Impact to Industry Accounting: Moderate

Wording to be Included in the Revenue Recognition Guide:

1. The intent of this paper is not to define the distinction between functional (i.e., point in time recognition) versus symbolic (i.e., over time recognition) licenses. Rather, this paper focuses on software licenses that a vendor has concluded are both functional and also distinct from other performance obligations in the contract. This paper will describe considerations an entity should consider in order to identify the specific point in time at which control transfers for these licenses.

2. When determining the point in time when control of a software license has transferred to the customer, in accordance with the indicators in FASB ASC 606-10-25-30 and ASC 606-10-55-58C, a software vendor may conclude that control has transferred to a customer once the customer has access to use the software code and also has the legal right to such use.

3. Software licenses are frequently delivered via access to the vendor's server, where the customer receives a password or key that allows the customer to download such software code to the customer's computing devices. Frequently in such situations, the vendor has no further contractual obligations related to the delivery of the license and the timing of when the customer takes possession of the software by using the provided password or key is entirely in the hands of the customer. As a result, FinREC believes that a vendor may conclude that control of a software license has transferred to a customer even though the customer has not taken possession of the software code by activating the password or key, based on the vendor's consideration of the other factors listed in FASB ASC 606-10-55-58-C and 606-10-25-30:
   a. The vendor has provided (or otherwise made available) the software to the customer.
   b. The period during which the customer is able to use and benefit from its right to access or its right to use the software has begun. For example, the entity would not recognize revenue before the beginning of the software license period even if the entity transfers the software code before the start of the license period or the customer has a copy of the software from a previous transaction. FASB ASC 606-10-55-58C also states, "For example an entity would recognize revenue from a license renewal no earlier than the beginning of the renewal period."
   c. The vendor has a present right to payment;
   d. The customer has the ability to direct the use of, and obtain substantially all of the remaining benefits from, the software

     e.   The customer has the significant risks and rewards of ownership of the asset; and the customer has accepted the software.

4. It may be helpful for software vendors to consider the specific wording of the customer contract when evaluating these factors. For example, if the contract includes a substantive acceptance requirement (e.g., in accordance with FASB ASC 606-10-55-87, the entity cannot objectively determine that the software provided to the customer is in accordance with agreed-upon specifications in the contract) and such acceptance has not yet occurred, the vendor should conclude that control of the licensed software has not yet transferred to the customer. Conversely, formal notification of customer acceptance may not preclude recognition if there are objective criteria for acceptance (as described in FASB ASC 606-10-55-86), and those criteria have been met, even if the customer has not formally accepted the software.

5. As mentioned in FASB ASC 606-10-55-58C, if a software license period begins before an entity provides (or otherwise makes available) to the customer a code that enables the customer to use the software, the entity would not recognize revenue before the beginning of the period to which the customer is able to use and benefit from the software and the code has been provided (or otherwise made available) to the customer.

6. Software vendors may also enter into transactions where software code is not delivered to a customer, but is maintained on the vendor's servers and the customer gets value from the use of that software, either through direct access to software that is hosted on a vendor's computers, or through a Software as a Service ("SaaS") offering to the customer. In some of these cases, a vendor may conclude that a license to the underlying software is a distinct performance obligation. This determination is not within the scope of this paper and is discussed in issue #14-1: Determining whether software intellectual property is distinct in cloud computing arrangements (i.e., hosting, software-as-a-service and hybrid cloud). The timing of the transfer of the underlying software code may be at the discretion of the customer and the vendor may or may not have active involvement in this transfer of the code. For example, a customer may be provided a key at the outset of the arrangement and the customer has the ability to download the software code from the vendor's server at any time. In other scenarios, a customer may have the right to use the software, and the software license period may have begun, but the customer may need to notify the vendor that it wishes to take possession of the software code and the vendor will then have to "push" the code to the customer upon receiving such notification. In these situations, while the transfer of the software has not yet occurred, the act of transferring such software may be *de minimus* and require minimal effort on the part of the vendor. A vendor should consider all of the relevant facts and circumstances to determine whether control of the software code has been transferred to the customer.

Comments should be received by August 1, 2017, and sent by electronic mail to Kim Kushmerick at kim.kushmerick@aicpa-cima.com, or you can send them by mail to Kim Kushmerick, Accounting Standards, AICPA, 1211 Avenue of the Americas, NY 10036.