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Proposed Accounting Standards Update, Technical Corrections and Improvements (File Reference No. 2016-220)

Dear Ms. Cosper:

We appreciate the opportunity to comment on the proposed Accounting Standards Update (ASU), Technical Corrections and Improvements. We support the effort by the Financial Accounting Standards Board (FASB or Board) to address feedback received from stakeholders on the Codification and to make other incremental improvements to US GAAP. For the most part, we agree that the proposed changes would clarify the Codification, correct unintended application of guidance or make minor improvements to the Codification that would not be expected to have a significant effect on current accounting practice or create a significant administrative cost to most entities.

However, we are concerned about certain of the proposed amendments as detailed below and have suggested other changes that are not included in the proposal.

► We agree that the technical corrections and improvements described in paragraphs 3-4 are necessary. We noted, however, that there are two definitions of Plan Assets in the master glossary; one is used in Accounting Standards Codification (ASC) 715-60 and ASC 965 and the other in ASC 715-30 and ASC 960. We are concerned that having two definitions may be confusing and recommend that the Board consider consolidating them. Specifically, we recommend removing the second definition of Plan Assets and adding the underlined text in the first definition as follows: “... to be used for a pension plan or a health and welfare plan (which can include active, terminated, and retired employees or their dependents or beneficiaries) ...” and “... the employer may intend that those assets be used to provide pension benefits or health and welfare benefits, which may include postretirement benefits.” Additionally, we recommend clarifying that the second paragraph in the definition of Plan Assets relates only to accounting by the plan sponsor because this paragraph states that nonbenefit obligations are considered reductions of plan assets, which doesn’t apply to accounting by the plan.

► We do not agree with the proposed amendments in paragraphs 11 through 14 because creating a glossary definition for Issued, Issuance, or Issuing of an Equity Instrument is confusing and could have unintended consequences because those terms are used differently throughout ASC 718, ASC 260 and ASC 505-50. Further, links to the master glossary are used inconsistently in these
sections. When a term is not linked to the master glossary, it could mean that the definition follows the first defined term in the section, or it could imply that the term has a different meaning (e.g., this term is sometimes used to mean “granted” when referring to unvested awards). Consider the following examples:

► Linking to the defined term “issued” in ASC 718-10-10-1, which states the objective of recognizing costs for share-based payments, could be confusing because share-based payments are never “issued” for awards for which a market condition is not achieved, but the compensation cost is still recognized.

► ASC 718-10-25-9 provides classification guidance for awards that are both vested and unvested. It appears that “issued” in this paragraph is really intended to mean “granted.” Defining “issued” could lead to an interpretation that this classification guidance does not apply to unvested awards. If the proposed definition is added to the master glossary, consider changing “issued” to “granted” in this paragraph to better reflect that this guidance applies to both vested and unvested awards. Similar changes may be needed in other paragraphs.

► ASC 718-10-15 does not contain links to the proposed master glossary term “issued.” As noted above, when a term is not linked to the master glossary, it could mean that the definition follows the first defined term in the section (though the term is not defined in section 718-10-15), or it could imply that the term has a different meaning (e.g., this term is sometimes used to mean “granted” when referring to unvested awards). Although there are no links to the master glossary term “issued” in 718-10-15, ASC 718-10-15-6 contains the term “issued” and seems to use it interchangeably with “granted.” This paragraph refers to share-based payment awards “issued” in a business combination, but this guidance applies to unvested awards as well. If the proposed definition is added to the master glossary, we recommend that the FASB consider changing “issued” to “granted” in this paragraph to better reflect that this guidance applies to both vested and unvested awards. Similar changes may be needed in other paragraphs.

► We believe that transition guidance should be provided for the proposed amendment to ASC 350-40 (paragraphs 31–32). Accounting Standards Update (ASU) 2015-05, Customer’s Accounting for Fees Paid in a Cloud Computing Arrangement, removed the requirement in ASC 350-40-25-16 to analogize to the leases guidance in ASC 840, Leases, when determining the asset acquired in a software licensing arrangement. With the removal of that analogy, we believe that the accounting for software licenses acquired for internal use following the adoption of ASU 2015-05 is not clear. Specifically, paragraph BC4 of ASU 2015-05 may suggest to some that licenses of software should be accounted for as executory contracts. It says “all software licenses in the scope of Subtopic 350-40 will be accounted for in the same manner, consistent with the accounting for other licenses of intangible assets” [emphasis added], and many licenses of intangible assets (e.g., licenses of intellectual property, including trademarks and patents) are accounted for as executory contracts in practice. For entities that have accounted for acquired internal-use software licenses as executory contracts following the adoption of ASU 2015-05, the proposed amendment that requires those licenses to be accounted for as intangible assets would result in a substantive change to that practice. In the absence of transition guidance, we would expect entities to apply the proposed amendment prospectively to new arrangements entered into subsequent to the issuance of this proposed ASU.
We suggest the following additional amendments to clarify the guidance on acquired internal-use software licenses:

- Paragraph BC5 of the proposed ASU states that “[t]he amendments in Update 2015-05, prescribe that an entity should apply the existing recognition and measurement requirements in GAAP for acquired intangible assets to a hosting arrangement that includes a license (as described in paragraphs 350-40-15-1 through 15-4C).” However, we fail to see this or a similar statement in reading ASU 2015-05. Therefore, we recommend that the Board clarify the language in the paragraph. We also suggest that the Board make clear in paragraph BC5 that the proposed amendment to ASC 350-40 does not apply to licenses of other intangible assets and should not be looked to by analogy.

- The proposed guidance in ASC 350-40-25-17 (paragraph 32) indicates that the acquisition of a license agreement for internal-use software should be accounted for as the acquisition of an intangible asset and the incurrence of a liability (that is, to the extent all or a portion of the software licensing fees are not paid on or before the acquisition date of the license). Some software license agreements include contingent or variable consideration (e.g., additional licensing fees payable related to the number of users of the licensed software). The proposed ASU clarifies that an acquired software license intangible asset should be recognized and measured in accordance with ASC 350-30-25-1 and 350-30-30-1, which references the asset acquisition guidance in ASC 805, Business Combinations. The asset acquisition guidance in ASC 805 is a cost accumulation model, under which an entity generally would not recognize a liability for contingent consideration in an asset acquisition until those costs have been paid or become payable, unless the contingent consideration meets the definition of a derivative. We think it would be helpful if the Board made it clear in ASC 350-40-25-17 that the recognition and initial measurement of an acquired software license intangible asset and the related liability would not include contingent or variable consideration.

- Software licensing agreements often include renewal periods beyond the noncancellable term. Any fees related to renewal periods would generally not be considered payable at the acquisition date. Thus, using the asset acquisition guidance in ASC 805 (and understanding analogies to ASC 840 have been removed), we do not believe renewal periods would be considered in the recognition and initial measurement of the acquired software license intangible asset and related liability. We think it would be helpful if the guidance clarified that renewal periods in a software licensing agreement would not be considered in the recognition and initial measurement of the intangible asset and liability in the acquisition of a software license.

- We recommend that the Board consider further amending ASC 715-30-35-88 (in paragraph 50) to add the underlined word to make the terminology consistent: “Accordingly, if a participating insurance contract requires or permits payment of additional premiums because of...”

- We agree with the Board’s decision (in paragraph 74) to replace the term “reinsurance receivable” with the term “reinsurance recoverable,” which historically referred to the unpaid portions of the assumed liability amounts but today is often used interchangeably with “reinsurance receivable.” However, we are concerned that the sentence describing them as the “same type of asset” could be confusing. Although a “reinsurance receivable” and “reinsurance recoverable” are both forms of financial assets, they are not the “same type of asset.” We therefore recommend that the Board remove the sentence from paragraph 74.
The asset described in ASC 815-15-55-101 (in paragraph 77) is the reinsurer's asset (i.e., the assuming entity) related to a modified coinsurance arrangement, as described in the illustrative example's Case B. The term “reinsurance recoverable” would be defined as “all amounts recoverable from reinsurers” (i.e., an asset of the ceding entity), so we recommend that the Board retain the language of “reinsurer's receivable” currently used in this paragraph. This would be consistent with the illustrative example, which describes the asset as a “funds-withheld receivable” (ASC 815-15-55-107).

Because the term “reinsurance recoverable” would incorporate both the paid and unpaid portions of the liability for claims amounts, we believe that ASC 944-40-50-3 (in paragraph 80) should be modified to clarify that the rollforward would include only the reinsurance recoverable related to unpaid claims amounts. We recommend that the Board modify ASC 944-40-50-3a to read: “and the related amount of reinsurance recoverable on unpaid claims.”

We suggest that the Board consider clarifying what constitutes “reinsurance recoveries” in ASC 944-40-55-6 (paragraph 81) to distinguish them from “reinsurance recoverables.” We believe the FASB intends to require disclosure of the amount of cash flows received, rather than those receivable, which would be clearer with the following change: “The information may also be presented before the effects of reinsurance with separate analysis of reinsurance recoveries (i.e., cash flows received) and reinsurance recoverables related to the incurred and paid amounts.

It is unclear to us why the FASB is proposing to change the language in ASC 944-605-55-1 (in paragraph 90) from “may” to “should.” Some entities may interpret the change as requiring them to offset balances if the criteria for “right of setoff” exist. This would change current practice, which allows but does not require insurers to present balances net when the criteria for a “right of setoff” exist. If the Board does not intend to change practice, we suggest retaining “may” to be consistent with similar guidance in ASC 210-20-45-2.

Paragraphs 106 and 107 of the proposed ASU would amend ASC 860-50-40-6 to include guidance in paragraph .08(h) of Statement of Position (SOP) 01-6 that was omitted from the Codification. The omitted guidance states that the carrying amount of servicing rights sold relating to loans that have been retained should be allocated at the date of sale between the servicing rights and the loans retained using relative fair values.

Statement of Financial Accounting Standards No. (SFAS) 166, which was issued after the guidance in SOP 01-6, defined the term “participating interest” and established specific conditions for reporting a transfer of a portion of a financial asset as a sale. One condition is that all cash flows received from the entire financial asset are divided among the participating interest holders in proportion to their ownership interests. Pursuant to ASC 860-10-40-6A.b.1, cash flows allocated as compensation for services performed, if any, are excluded from the cash flows required to be allocated proportionately to participating interest holders if payment for such services is:

i. Not subordinate to the proportionate cash flows allocated to the participating interest holders

ii. Not significantly above an amount that would fairly compensate a substitute service provider, should one be required, which includes the profit that would be demanded in the marketplace (i.e., “adequate compensation,” as defined in the master glossary)
Servicing fee payments that are significantly above adequate compensation entitle the recipient to a disproportionate interest in the contractual cash flows of the underlying financial asset, meaning they wouldn’t meet the definition of a participating interest.

If the FASB intends the proposed amendment to apply when servicing fees do not meet the conditions specified in ASC 860-10-40-6A.b.1(i) and b.1(ii), we suggest that the Board make conforming amendments to the unit of account eligible for derecognition guidance in ASC 860-10. If not, we suggest that the Board clarify the circumstances in which the proposed guidance would apply. Also, we suggest that the accounting for arrangements that do not meet the requirements specified in ASC 860-10-40-6A.b.1 be clarified as follows:

- Continue to recognize the servicing rights with no change in measurement
- Account for the collateral pledged in accordance with ASC 860-30-25-5
- Recognize the cash or other consideration received as an asset and an offsetting liability
- In subsequent periods, amortize the liability in proportion to and over the period of estimated net servicing expense

The proposed ASU (paragraphs 120–121) would update the example in ASC 946-210-55-1 to be consistent with paragraph 7.229 in the Guide. We believe the following minor editorial changes would make the proposed guidance clearer:

- Add a comma to the title of the first column header in the illustrative example: “Principal Amount, Shares, or No. of Contracts:”
- Consistently use periods instead of commas to separate the decimal places in all percentage of net assets disclosures (e.g., Futures Contracts – Financial 5.2% rather than 5,2%)

The proposed addition of ASC 958-605-15-13 (in paragraph 131) does not seem necessary to clarify the scope of the Transfers subsections in ASC 958-605. The guidance in ASC 958-605-05-4 and 958-605-15-10 describes that scope as “transfers ... for which ... a donor uses a recipient entity ... to transfer assets to a third-party donee.” A transfer to an affiliated recipient entity (or any recipient entity) that is also the beneficiary would not be within that scope. If the new guidance is retained, we suggest that it be added instead as paragraph ASC 958-605-15-10A, so that it directly follows the discussion of which transactions are within the scope of these subsections.

We believe the guidance for transfers to affiliates would be clearer if errors in the flowchart in the implementation guidance (in ASC 958-605-55-74) related to transfers to an affiliate were corrected to make it identical to the one the FASB issued in SFAS 136, Transfers of Assets to a Not-for-Profit Organization or Charitable Trust That Raises or Holds Contributions for Others. The codified flowchart is missing the question, “Does the resource provider specify itself or its affiliate as the beneficiary?” (The previous question is listed twice in error instead.) In addition, the decision tree question, “Does the transfer meet all of the criteria in paragraphs 958-20-25-4 through 25-7 (an equity transaction)?,” provides two “yes” paths and does not have a “no” path.
ASC 958-810-45-1 addresses presentation of noncontrolling interests in the statement of financial position, whereas ASC 958-810-50-4 through 50-5 address disclosure of a schedule of changes in consolidated net assets attributable to the parent and the noncontrolling interest, which can be provided in the statement of activities or in the notes. The proposed amendment to ASC 958-810-45-1, as explained by paragraphs 134 and 135 of the proposal, would be clearer if it said: “See paragraphs 958-810-50-4 through 50-5 for additional guidance on the requirement related to disclosure of changes in consolidated net assets attributable to the parent and the noncontrolling interests, which may be provided either on the face of the statement of activities or in the notes.”

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We would be pleased to discuss our comments with the Board members or the FASB staff at your convenience.

Very truly yours,

[Signature]
Ernst & Young LLP