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**File Reference No. 1820-100 Exposure Draft of a Proposed Accounting Standard Update -
*Revenue from Contracts with Customers***

The Financial Reporting Executive Committee (FinREC), formerly known as the Accounting Standards Executive Committee (AcSEC), of the American Institute of Certified Public Accountants appreciates the opportunity to comment on the Exposure Draft of the Proposed Accounting Standards Update, *Revenue from Contracts with Customers* (the Exposure Draft). FinREC supports the boards' overall goal of creating a single revenue recognition model and also supports the objectives of the Exposure Draft. While the boards have made considerable progress since issuance of the 2008 Discussion Paper, we believe further consideration and deliberation is warranted as we do not believe the boards' objectives have yet been fully achieved. We therefore respectfully request that the boards and their respective staffs consider the following observations:

Identifying the contract(s) with a customer

We agree with the proposed definition of a contract. However, we believe that the governing principle for the accounting for contract combinations, segmentation and modifications should be based on the economics of the transaction and not solely on price considerations.

We believe that contracts (including contract modifications) should be combined when the facts and circumstances surrounding their negotiation indicate they are economically or functionally interdependent. We believe the indicators of interdependence should be amended to include price and also address the additional concepts of economic and functional interdependence.

We do not believe it is necessary to have both a contract segmentation principle and a separation of performance obligations principle. The proposed standard is focused on performance obligations. We therefore believe that a segmentation principle is unnecessary provided that certain amendments are made to the existing principle for performance obligations. Our response to Questions 1 and 4 further describes our concerns. If the boards should decide to include a contract segmentation principle, we believe a contract should be segmented when the facts and circumstances surrounding its negotiation indicate that the contract's segmented components are economically or functionally independent.

We believe the proposed contract modification guidance may not be operational. In addition to the challenges of using price interdependence to determine the accounting for contract modifications, we believe there may be circumstances when prospective treatment of contract modifications (rather than cumulative treatment as proposed) may better reflect the transaction economics. Accordingly, we believe that companies should account for the effect of a modification either on a prospective or cumulative basis, depending upon which measure is supported by the underlying economics of the transaction and provides more decision-useful information.

Identifying the separate performance obligations in the contract

We agree with the principle of a performance obligation and that separate performance obligations represent a reasonable basis for revenue recognition. However, the principles outlined in paragraphs 22 and 23 require further clarification. We believe the subsequent definitions and concepts used in the guidance and basis for conclusions do not sufficiently articulate the principle. We believe the proposed definition of "distinct", without further refinement, is too imprecise for implementation and could result in inconsistent application or may result in separating performance obligations at a level lower than that which would provide decision-useful information. We believe the boards need to improve the proposed principle to ensure that a final separation principle is operative and results in accounting results that reflect the economics of the transactions across industries and contracts.

Determination of the transaction price

We agree with the proposal that revenue recognition should be based on the estimation of the overall transaction price when consideration is variable. The application of this principle, however, has several practical limitations that must be addressed in the final standard. We encourage the boards to carefully consider the following:

- We believe alternative methods to the estimation process should be permitted. The theoretical merits of the proposed probability-weighted approach are sound; however, other alternatives, such as a best estimate methodology, might better reflect the economics of certain transactions and may be more cost-effective to implement. We believe therefore that companies should be required to apply a best estimate methodology which could include a probability weighted approach. We believe this will provide more decision-useful information.
- The transaction price should reflect customer credit risk provided such risk is reliably measureable. We do not believe, however, that subsequent changes to the original credit risk estimation should be reflected in a manner other than as an adjustment to revenue. We believe all adjustments to the estimated transaction price should be reflected in revenue to ensure consistency.
- We believe in the theory of applying the time value of money in situations where customer or vendor financing is an integral part of the negotiations between the parties to the transaction. Where material, we believe the consideration of time value of money is appropriate. We recommend that the boards develop a framework for applying the time value of money, to provide a consistent objective for determining how an appropriate discount rate should be selected, as we believe this issue is fundamental and far reaching beyond the revenue recognition project. We acknowledge the concept of materiality is an individual judgment that is highly subjective. The boards should consider whether a practical expedient may permit companies to appropriately focus on materiality judgments.
- Consideration paid to a customer should be reflected as a reduction of the transaction price. Payments to a customer that relate specifically to goods or services which the vendor could have procured independent of the customer sales transaction warrant a different accounting treatment. Provided the transactions are substantive, companies should reflect the accounting for such customer consideration through other applicable accounting guidance.

Allocate the transaction price to the separate performance obligations

We agree that actual or estimated standalone selling prices of performance obligations should be used in the allocation of the transaction price. We believe existing estimation methodologies will allow entities to derive the standalone selling prices where independently observable measures may not exist.

Recognize revenue when a performance obligation is satisfied

We agree with the principle that revenue should be recognized when a performance obligation is satisfied. Additional guidance, however, is necessary to assist in determining when control transfers; in particular for services and goods that transfer continuously to the customer. We have therefore provided additional indicators of control transfer which we believe merit consideration. We also believe that, in situations where control transfers continuously during the contract, entities should use a measurement methodology that best reflects the economics of the transaction and suggest that the proposed guidance may be overly biased toward the use of output measures. We believe that for many contracts for which control transfers continuously, an input measure (e.g., proportion of costs incurred) may be an appropriate and practical reflection of control transfer to the customer.

Additional considerations

We do not believe the proposed revenue standard should provide guidance for the accounting for contract costs. Onerous performance obligations, contract acquisition costs, and fulfillment costs should be part of a more comprehensive consideration of cost guidance by the boards. Until such time as the boards undertake such a project, we support the proposed principles outlined in the Exposure Draft, with some important modifications.

We believe the onerous assessment should be applied at the contract level unless the economics of the transaction or customer relationship warrants the consideration either at the performance obligation level or to a combination of contracts. The proposal by the boards is overly prescriptive and may not ultimately reflect consideration of the negotiated economics.

We believe the concepts of abnormal and learning curve costs require further deliberation and definition to ensure a consistent application of the boards' intention.

A comprehensive disclosure framework is an imperative that requires the immediate attention of the boards as each of the joint FASB / IASB projects is attempting to address the need for expanded disclosures of decision-useful information. We believe the proposed disclosures described in this Exposure Draft are excessive in scope and require a level of detail that will obscure the information that the users of financial statements find necessary and desirable. Accordingly, we believe a concerted and comprehensive approach to disclosure will provide the opportunity for improvement in a meaningful and balanced way.

We acknowledge the retrospective application approach would enhance the inter-period comparability of financial information provided it is reliably recreated and consistently applied. However, we challenge whether this goal is attainable given the complexity and long-term nature of many contracts; including those containing modifications and multiple element arrangements. We also believe the proposal is not consistent with the methodologies proposed in other Exposure Drafts and projects underway. The boards should carefully consider the impact of alternative adoption methodologies of the various Exposure Drafts (e.g., prospective or modified prospective transition). We question how useful the financial statements and footnotes of a company will be when applying multiple standards, each with differing transition methods of adoption.

Throughout the Exposure Draft there are numerous lists of factors, criteria or indicators that support the principles therein. We suggest the boards consider adding language in all such cases clarifying that these lists are neither determinative nor exhaustive.

Several of the existing Exposure Draft examples should be replaced or amended with those accumulated through the boards' outreach activities. We understand that there have been an overwhelming number of examples provided, across diverse industries, and suggest that several of those examples may be suitable replacements to existing examples. We encourage the boards to collaboratively develop these examples with constituents across all industries.

We agree with the theoretical merit of many of the concepts included in the proposed standard. We also believe, however, that certain principles, as proposed and further discussed below, may be neither practical nor operational for preparers and auditors to apply without undue cost. We therefore encourage the boards to carefully weigh the cost-benefit implications of certain of these principles as a final standard is developed.

We believe that based on the outcome of re-deliberation by the boards, re-exposure of the proposed standard should be strongly considered to ensure sufficient and appropriate due process has been provided to those impacted by the Exposure Draft.

Our answers to the specific questions in the Exposure Draft provide more detail on the views expressed above and are attached in the Appendix to this letter.

Yours faithfully,

Jay Hanson, Chair

Financial Reporting Executive Committee

Dan Zwarn, Chair

Revenue Recognition Comment Letter Task Force

Exposure Draft on Revenue from Contracts with Customers

Question 1

Paragraphs 12-19 propose a principle (price interdependence) to help an entity determine whether to:

- (a) combine two or more contracts and account for them as a single contract;*
- (b) segment a single contract and account for it as two or more contracts; and*
- (c) account for a contract modification as a separate contract or as part of the original contract.*

Do you agree with that principle? If not, what principle would you recommend, and why, for determining whether (a) to combine or segment contracts and (b) to account for a contract modification as a separate contract?

We believe that economic and functional interdependence are important to the process of defining the contract. We believe that pricing considerations should be viewed as a factor in this overall analysis and not the sole definition of the principle. Functional and economic interdependence are concepts within existing literature that we believe should be the foundations for the principle used to determine when it may be appropriate to combine contracts (including contract modifications). We therefore encourage the boards to consider the following amended principle:

An entity shall combine two or more contracts and account for them as a single contract if the goods or services in one contract are economically or functionally interdependent with the goods or services in another contract.

While paragraph 13 already provides sound indicators of when such interdependence may be achieved (i.e., the contracts are entered into at or near the same time; the contracts are negotiated as a package with a single commercial objective; and the contracts are performed either concurrently or consecutively), consideration should be given to additional indicators such as:

- *The price of contracts are interdependent, for example:*
 - *The fee for one or more contracts is subject to refund of forfeiture or other concession if another contract is not satisfactorily completed*
 - *Payment terms under one contract coincide with performance criteria of another contract*
 - *One or more obligations in a contract is essential to the functionality of an obligation in another contract*

We understand the rationale for requiring contract segmentation is to address the allocation of contract consideration to the performance obligations to which it most closely relates. However, we do not believe that having both a contract segmentation principle and a performance obligation separation principle is necessary to reflect the economics of the transactions and therefore suggest that the segmentation requirement should be removed. If the boards proceed with a segmentation principle, however, we believe amendments are required. The proposed segmenting guidance outlined in paragraph 15 provides prescriptive conditions for when segmentation must be performed but we believe this is inconsistent with the principles-based objectives of the Exposure Draft. As with contract combinations, we believe that any contract

segmentation principle should be based on economic and functional independence, rather than just price considerations. The guidance should permit judgment for when the economics of a transaction represents two independent transactions or a single transaction.

We believe the modification principle within the proposed guidance may not be operational. Specifically, and consistent with our concern around the proposed combination principle, we believe that economic or functional interdependence (rather than only price interdependence) should govern when modifications are to be combined with the original contract or accounted for separately. We believe the factors used for determining price interdependency are biased to transactions "entered into at or near the same time". The proposed principle, and additional indicators outlined above, assists in reducing this bias and clarifying this ambiguity.

The boards have suggested the effect of all modifications should be accounted for on a cumulative basis. We believe there may be circumstances in which prospective treatment might be a better representation of the economics of a particular transaction. We believe that companies should be provided with guidance that outlines when it may be appropriate to prospectively account for the effect of a modification and when a cumulative basis would be appropriate. In addition, certain modifications, such as unpriced change orders, require an assessment as to whether both the definition of a contract and the contract modification principles are met. We encourage the boards to provide application guidance as to how the modification principle would apply to this, and other unique contract modifications.

We also suggest the boards consider whether greater clarification is needed for the definition of a contract modification and for contract options. Many have suggested that the proposed guidance is unclear. We suggest that a contract modification is the result of a subsequent substantive renegotiation of a contract whereas a contract option is included in the terms of the original contract.

Question 2

The boards propose that an entity should identify the performance obligations to be accounted for separately on the basis of whether the promised good or service is distinct. Paragraph 23 proposes a principle for determining when a good or service is distinct. Do you agree with that principle? If not, what principle would you specify for identifying separate performance obligations and why?

We agree with the proposed performance obligation principle and that separate performance obligations represent a reasonable basis for revenue recognition. However, the principles outlined in paragraphs 22 and 23 require further clarification. We believe the subsequent definitions and concepts used in the guidance and basis for conclusions do not sufficiently articulate the principle. Central to these concerns is the proposed requirement to have a "distinct function" and a "distinct margin." We believe that such a requirement will result in inconsistent application and may, in many circumstances, not be a relevant factor. For example, we have difficulty envisioning a good or service that literally has no utility either by itself or in conjunction with other goods or services. As such, we believe the boards need to improve the proposed principle to ensure that a final separation principle is operative and results in appropriate accounting that reflects the economics of the transactions across industries and contracts.

In considering the method for separating performance obligations, we are unclear on whether the boards' intent is to require companies to first identify all performance obligations in a contract and then determine subsequent aggregation (a bottom up approach), or whether companies are required to identify only those performance obligations that require separation (a top down

approach). We support the "top down" approach and believe that, without further clarification, the boards' proposal may result in inconsistent application of this principle.

In the event the boards proceed with the current definition of a performance obligation, we believe it is imperative the following modifications be made in order to ensure consistent application:

- Paragraphs BC50 and BC53-56 includes definitional distinctions critical to the rules outlined in paragraphs 22 and 23 and should be considered for inclusion in a final standard.
- Paragraph BC55 requires that an entity must separately identify the resources needed to provide the good or service. A strict interpretation of this rule would suggest that if the exact same resource is used to satisfy more than one performance obligation, separation is not permitted. We believe the use of similar resources should not be a factor in determining the separation of performance obligations.
- The concepts for contract management services in paragraphs BC57 - BC58 should be included within the final guidance and supplemental examples should be provided to assist in the explanation of the intended application of the principle.

Question 3

Do you think that the proposed guidance in paragraphs 25-31 and related application guidance are sufficient for determining when control of a promised good or service has been transferred to a customer? If not, why? What additional guidance would you propose and why?

We agree with the principle for the transfer of control as outlined in paragraphs 25-31. We believe, however, that additional indicators are needed. We therefore offer the following additional indicators:

Additional indicators of continuous transfer of control may include, but are not limited to:

- The customer may restrict the use of the deliverable or the design of a particular deliverable.
- The customer is entitled to the incomplete deliverable or has the ability to seize work-in-progress (with or without penalty)
- Dedicated resources have been identified by the vendor to a particular order for a particular customer

Additional indicators of control transfer at a point in time may include, but are not limited to:

- The vendor retains a unilateral ability to substitute identical products for transfer to a variety of customers
- The vendor retains the right to determine product design specifications and to change design specifications

We agree with the principle for the transfer of control and the proposed measurement metrics but recommend the entity use the methodology that best represents the economics of the transaction(s). In considering the guidance within paragraphs 32 - 33 and BC74, we note there appears to be a bias toward the use of output measures to depict the transfer of control. We agree that such measures would seem appropriate where available and objectively determinable. However, we also believe that other methods (e.g., input methods such as those articulated in

paragraph 33b) should be permitted if output measures do not best reflect the underlying economics of the transaction.

Question 4

The boards propose that if the amount of consideration is variable, an entity should recognize revenue from satisfying a performance obligation only if the transaction price can be reasonably estimated. Paragraph 38 proposes criteria that an entity should meet to be able to reasonably estimate the transaction price.

Do you agree that an entity should recognize revenue on the basis of an estimated transaction price? If so, do you agree with the proposed criteria in paragraph 38? If not, what approach do you suggest for recognising revenue when the transaction price is variable and why?

We agree that revenue recognition should be based on an estimation of the ultimate transaction price when consideration is variable. We believe the proposed guidance and the related criteria in paragraph 38 represent an appropriate basis for the determination of the estimated transaction price. We believe, however, that in certain circumstances there may be a practical limitation in obtaining "access to the experience of other entities" and therefore suggest that entities be permitted (where appropriate) to use "sufficient history of similar transactions" from which a reasonable estimate can be made if access to the experience of other entities is impracticable to attain. We also believe that the boards should clearly indicate that the factors of a relevant history outlined in paragraph 39 are not exhaustive and that other factors may be relevant to such a determination.

We also believe that the boards should consider whether alternative transaction price estimation methods should be permitted. While we acknowledge the merits of the suggested probability-weighted approach, we believe alternative approaches, for example a best estimate approach, might better reflect the economics of certain transactions (e.g., when the amount of cash to be received is binary). We are troubled by an estimation methodology that yields an outcome that does not reflect the economics of the transaction and therefore suggest greater latitude be permitted. We also believe that in certain circumstances there may be practical difficulties in implementing a probability weighted approach to individual transactions. Therefore, we believe the boards should modify the proposed guidance to require the use of a best estimate approach, which could include the use of a probability-weighted methodology.

We agree with the principle that consideration paid to a customer should be reflected as a reduction of the transaction price unless the payment relates specifically to goods or services which the vendor would have procured independent of the sales transaction with the customer.

Question 5

Paragraph 43 proposes that the transaction price should reflect the customer's credit risk if its effects on the transaction price can be reasonably estimated. Do you agree that the customer's credit risk should affect how much revenue an entity recognizes when it satisfies a performance obligation rather than whether the entity recognizes revenue? If not, why not?

We agree that the transaction price should reflect customer credit risk provided such risk is reliably measureable. We do not believe, however, that subsequent changes to that estimate should be reflected in other income or expense. We believe all adjustments to the transaction price should be reflected in a consistent manner. We believe any changes in the transaction

price, whether related to variable consideration, customer credit risk or otherwise, should be reflected in revenue. This is especially important because users of financial statements are interested in reconciling revenue with the amount of cash received.

We believe the boards should provide clarity in the application of reasonably estimated and whether the intended principle is applicable for all transaction price inputs.

Question 6

Paragraphs 44 and 45 propose that an entity should adjust the amount of promised consideration to reflect the time value of money if the contract includes a material financing component (whether explicit or implicit). Do you agree? If not, why?

We believe in the conceptual merits of applying the time value of money in situations where a material financing element between the parties exists. We do not believe that the differences between the timing of payments and the satisfaction of performance obligations should mandate the calculation of the time value of money in all circumstances. For example, we would suggest it is appropriate to apply the time value concept to transactions where a payment is due in excess of 12 months or outside the normal and customary vendor terms after control of the good or service transfers. We do not believe that it is always appropriate to adjust the transaction price when amounts are paid in advance, as some prepayments do not represent a financing element but are simply a function of the customer's budget cycle and payment process or intended to provide a customer with protective rights. As proposed, vendors must record revenue accretion (imputed interest income) on advance payments but this accretion does not represent a future cash flow obligation of the customer. Similarly, vendors must record "interest expense" to offset the revenue accretion but this "expense" does not represent a future cash outflow obligation of the vendor. The boards' approach involves offsetting increases to revenues and expenses that are not grounded in transaction economics or cash flows.

We also believe that practical challenges will arise as entities develop systems to calculate the time value of money on all contracts, especially those with multiple deliverables and long-term arrangements. We believe in many circumstances the implementation and application costs will outweigh the ultimate benefit to users of those financial statements.

Question 7

Paragraph 50 proposes that an entity should allocate the transaction price to all separate performance obligations in a contract in proportion to the stand-alone selling price (estimated if necessary) of the good or service underlying each of those performance obligations. Do you agree? If not, when and why would that approach not be appropriate, and how should the transaction price be allocated in such cases?

We agree with the principle of allocating the transaction price in proportion to the stand-alone selling price of the good or service underlying each performance obligation. The various industry representatives on our task force believe that the proposal is operational given their efforts in adopting Accounting Standards Update No. 2009-13, Revenue Recognition (Topic 605): *Multiple-Deliverable Revenue Arrangements*. We believe established estimation methodologies will permit entities to appropriately estimate stand-alone selling prices and therefore support the proposal. The recent adoption of ASU No. 2009-13 has demonstrated this.

We also believe the boards should consider including the guidance in paragraph BC125 within the final standard. We believe that, provided a company has conducted an exhaustive analysis of alternative measures of standalone selling price, the residual technique may be an appropriate alternative of last resort.

In considering the estimation alternatives outlined in paragraph 52 of the proposed standard, we believe the boards should clearly indicate that such a list is not exhaustive of the alternatives available and suggest the modification of the language as follows:

"When estimating stand alone selling prices, an entity shall maximize the use of observable inputs and shall apply estimation methods consistently for goods or services and customers with similar characteristics. Suitable estimation methods include, but are not limited to, the following..."

Question 8

Paragraph 57 proposes that if costs incurred in fulfilling a contract do not give rise to an asset eligible for recognition in accordance with other standards (for example, IAS 2 or ASC Topic 330; IAS 16 or ASC Topic 360; and IAS 38 Intangible Assets or ASC Topic 985 on software), an entity should recognize an asset only if those costs meet specified criteria.

Do you think that the proposed requirements on accounting for the costs of fulfilling a contract are operational and sufficient? If not, why not?

We believe a revenue standard should not provide guidance on the accounting for contract costs; rather, a more comprehensive consideration of cost guidance should be undertaken by the boards. We recognize, however, that existing revenue guidance, such as ASC 605-35 (formerly SOP 81-1), includes significant cost guidance and the absence of such guidance would create a significant void. We therefore support the proposed cost principle outlined within the Exposure Draft until such time that a comprehensive review of cost guidance is undertaken. The boards must, however, carefully consider the need for consequential amendments to this or other existing cost standards to address potential inconsistencies.

If the boards decide to continue with this approach, we believe certain adjustments should be made as follows:

- Additional application guidance and more examples of what costs might be eligible for capitalization under paragraph 57
- Clarity in paragraph 58(a) as to whether direct labor costs are "fully loaded" with an allocation of overhead
- Reword paragraph 58(e) to prevent it from being too broadly interpreted
- Clarity as to what specifically constitutes learning curve costs

There is also a need for greater clarity of what constitutes abnormal costs. We believe the concept within this Exposure Draft is maybe intended to be consistent with the principle of abnormal costs outlined in ARB 43 Chapter 4 Statement 3, which is specific to inventory allocation costs. We generally support the concept that abnormal costs should be expensed as incurred. We believe, however, a more thorough definition, coupled with application indicators and examples, is required.

We suggest the following could be indicators of costs that may not be abnormal:

- Additional costs that result from the renegotiation (or modification) of a contract that are recoverable, either through the original transaction consideration or through supplemental payments made by the customer
- Cost estimate revisions for previously identified and estimated costs that were considered in developing the original cost estimates (e.g., labor costs are now 120% of prior estimates)

We suggest that the following could be indicators of costs that may be abnormal:

- Additional variable production overhead costs allocated to units of production as a result of abnormally low production levels
- Additional fulfillment costs that were not considered in the original bidding process and that will not be reimbursed by the customer.

While these are only a sample of the indicators of each, we believe a more thorough definition and supporting indicators are essential.

We also believe the boards should reconcile the accounting for contract costs between this and other proposed standards. The proposed leases standard, for example, requires certain acquisition costs to be capitalized as part of the right-of-use asset, whereas the proposed revenue standard requires all such costs be expensed as incurred.

Question 9

Paragraph 58 proposes the costs that relate directly to a contract for the purposes of (a) recognizing an asset for resources that the entity would use to satisfy performance obligations in a contract and (b) any additional liability recognized for an onerous performance obligation.

Do you agree with the costs specified? If not, what costs would you include or exclude and why?

We agree with the cost categories provided in paragraph 58. We would, however, suggest the modification of subparagraph 58(e). We believe the proposed wording, "costs that were incurred only...." is vague and may be too broad. We therefore suggest this category be reworded or eliminated in its entirety. We also recommend that the Exposure Draft clarify whether direct costs relate solely to a specific contract or to a series of contracts with a particular customer.

We do not believe that guidance for onerous performance obligations should be included within the proposed standard; rather such guidance should be included in a more comprehensive cost project. In the event the boards proceed with the inclusion of such guidance within this standard, we believe that an onerous test should be applied at the contract level unless the economics of a transaction or customer relationship warrants consideration either at the performance obligation level or to a combination of contracts. If the boards affirm their proposal to assess whether a performance obligation (as opposed to the entire contract) is onerous, another approach that could be considered would be to modify the criteria in paragraph 57 for capitalized contract costs to allow deferral and attribution of an onerous performance obligation "loss" over the period that revenue from other performance obligations is recognized. In other words, one might view the loss as a contract investment or as an "inventoriable charge" under FASB ASC 330-10.

Question 10

The objective of the boards' proposed disclosure requirements is to help users of financial statements understand the amount, timing and uncertainty of revenue and cash flows arising from contracts with customers. Do you think the proposed disclosure requirements will meet that objective? If not, why?

We believe the development of a comprehensive disclosure framework is necessary in order to provide decision useful information for users of financial statements. The proposed disclosure requirements include many specific and detailed disclosures that we believe are excessive and will likely obscure the information that financial statement users will find necessary and useful.

We believe the inclusion of predictive or forecasted information within the financial statement notes will present significant challenges given that this prospective information, irrespective of the amount of diligence used in its creation, is inherently prone to error, diverse interpretation, and inter-temporal volatility, which will likely reduce its usefulness. The inclusion of prospective information will also challenge preparers given their limited ability to support key assumptions about future events and the potentially high legal exposure associated with the inclusion of such information in financial statements. We believe that predictive disclosures may be more useful when included in other documents that are subject to appropriate Safe Harbor provisions.

Through our analysis we noted that similar predictive disclosures are not required by other existing or currently proposed standards. In addition, concepts such as "backlog", which may be used in order to develop these disclosures, may not be defined on a consistent basis and could result in decreased comparability amongst reporting entities.

We suggest the disclosure principles be clarified to focus on the overarching objectives of the disclosure and the key judgments and estimates associated with accounting for contracts with customers.

Question 11

The boards propose that an entity should disclose the amount of its remaining performance obligations and the expected timing of their satisfaction for contracts with an original duration expected to exceed one year.

Do you agree with that proposed disclosure requirement? If not, what, if any, information do you think an entity should disclose about its remaining performance obligations?

We do not believe these proposed disclosures should be required within the financial statement footnotes. This information is predictive in nature and is subject to significant and potentially unsupported assumptions regarding the timing and extent of a customer's future needs and requests. We further believe that, even with a comprehensive analysis, these estimates will be unreliable and extremely time sensitive. Consistent with our views on Question 10, we believe such disclosures may not provide decision useful information to financial statement users and an entity should not be required to disclose forecast information in audited financial statements.

Question 12

Do you agree that an entity should disaggregate revenue into the categories that best depict how the amount, timing and uncertainty of revenue and cash flows are affected by economic factors? If not, why?

It's difficult to reject a principle that suggests disclosures that "best depicts the amount, timing and uncertainty of revenue and cash flows..." If the disaggregated information is readily attainable, reliably measureable, is useful, and permits a company to disclose key judgments and estimates in a manner not detrimental to their competitiveness or at undue cost, we believe it should be disclosed. Discretion, however, should be provided to permit disclosures to be viewed from management's perspective and to minimize, where possible, the inevitable second guessing of such disclosures. We recommend some parameters be established that limit the amount of disaggregated information to an appropriate level. We considered whether the notion of the Chief Operating Decision Maker within current segment reporting guidance could provide the appropriate perspective and serve as a means for limiting the amount of disclosure to readily available, decision useful information that is consistent with how senior management manages the business. We offer the following suggested amendments to paragraph 74:

An entity shall disaggregate revenue into categories that are used by the Chief Operating Decision Maker which ...

Question 13

Do you agree that an entity should apply the proposed requirements retrospectively (i.e., as if the entity had always applied the proposed requirements to all contracts in existence during any reporting periods presented)? If not, why?

Is there an alternative transition method that would preserve trend information about revenue but at a lower cost? If so, please explain the alternative and why you think it's better.

We acknowledge that retrospective application would enhance the inter-period comparability of financial information provided it was reliably recreated and applied consistently. We are concerned, however, that given the complexity and duration of many contracts, preparers of financial statements may not be able to accurately determine the necessary contract information to apply the proposed standard on a retrospective basis.

We understand a number of other Exposure Drafts have considered and rejected retrospective application as being unreliable. Several participants in those debates have indicated that the long-term nature of certain contracts, and the inability of preparers to accurately recall the inputs and information as of those prior dates, make such an option unreliable. Such factors are not unique to transactions within the scope of those Exposure Drafts and we believe those arguments hold true for the revenue Exposure Draft.

Many entities may transact within a single contract to provide deliverables that fall within the scope of the various Exposure Drafts. We wonder how useful prior information will be to readers of financial statements if the historical financial results are presented through the kaleidoscope of, for example, revenue, leasing, financial instruments, and insurance literature, each with different methods of adoption.

We believe that decision-useful financial information could be provided if the boards permitted alternative adoption methodologies for the respective Exposure Drafts which would allow the entities to appropriately consider their particular circumstances and provide transition information

in a harmonious manner. We believe requiring entities to adopt these standards contemporaneously prior to a not-to-exceed date will accomplish this. We also believe that supplemental information, similar to that required by ASU 2009-13 and 14, will enable readers to provide investors with sufficient and appropriate transition information.

Question 14

The proposed application guidance is intended to assist an entity in applying the principles in the proposed requirements. Do you think that the application guidance is sufficient to make the proposals operational? If not, what additional guidance do you suggest?

We believe significant application guidance will be required to assist entities in applying the judgment required by this Exposure Draft. While current application guidance, in certain instances, is helpful in making the proposed concepts operational in certain instances, the application guidance is too simplistic. We also believe that many individuals and organizations have already begun interpreting the concepts in a manner that was either not intended or in an inconsistent manner. In most cases a contract exists for certain activities, such as research studies under a federal grant or clinical trials for others. It is unclear what activities within this example are within the scope of the proposed standard.

We therefore suggest that several of the existing examples be replaced or amended with those accumulated through the boards outreach activities. We understand that there have been an overwhelming number of examples provided, spanning diverse industries, and suggest that several of those examples may be suitable replacements. We encourage the boards to collaboratively develop these examples with constituents across all industries.

Many preparers and readers of the financial statements have voiced their concerns that the highly judgmental decisions have been left to the written and unwritten interpretations of a few parties; specifically regulators and audit firms. We therefore believe that more complex examples will help to capture the incredible wealth of information accumulated by the boards and provide the appropriate interpretations that memorialize the efforts of this process.

Question 15

The boards propose that an entity should distinguish between the following types of product warranties:

- (a) a warranty that provides a customer with coverage for latent defects in the product. This does not give rise to a performance obligation but requires an evaluation of whether the entity has satisfied its performance obligation to transfer the product specified in the contract.*
- (b) a warranty that provides a customer with coverage for faults that arise after the product is transferred to the customer. This gives rise to a performance obligation in addition to the performance obligation to transfer the product specified in the contract.*

Do you agree with the proposed distinction between the types of product warranties? Do you agree with the proposed accounting for each type of product warranty? If not, how do you think an entity should account for product warranties and why?

We believe the boards' proposal for the accounting for product warranties is conceptually pure but will be impracticable to apply for the following reasons:

- Many companies do not track the specific nature of the underlying warranty services provided
- Companies often sell warranty services that do not distinguish between latent defects and insurance-type warranties
- There are significant operational challenges and costs to implement an appropriate tracking system

We therefore believe that a single warranty model should be adopted as a practical expedient and believe that the existing model is appropriate. In the absence of a model that preserves the existing cost accrual model, we would recommend the guidance permit warranties to be accounted for as separate performance obligations where companies could apply a cost plus reasonable margin to determine the appropriate allocation of consideration to that separate warranty obligation.

Question 16

The boards propose the following if a licence is not considered to be a sale of intellectual property:

- (a) if an entity grants a customer an exclusive licence to use its intellectual property, it has a performance obligation to permit the use of its intellectual property and it satisfies that obligation over the term of the licence; and*
- (b) if an entity grants a customer a non-exclusive licence to use its intellectual property, it has a performance obligation to transfer the licence and it satisfies that obligation when the customer is able to use and benefit from the licence.*

Do you agree that the pattern of revenue recognition should depend on whether the licence is exclusive? Do you agree with the patterns of revenue recognition proposed by the boards? Why or why not?

In our review of the proposed accounting for the sale of intellectual property, we noted the proposal appeared to be a prescriptive solution to a number of difficult revenue scenarios. This perception may stem from the difficulty we had in determining the actual performance obligation for an exclusive license when the term was for less than the economic useful life of the underlying asset. We therefore do not agree with the exclusivity "bright line" that is currently being proposed and believe that both exclusive and non-exclusive licenses should be accounted for in the manner proposed for non-exclusive licenses, which we believe is consistent with the principles in the proposed standard. If the boards retain separate revenue recognition requirements for exclusive and non-exclusive licenses, we would suggest that additional consideration should be given to providing indicators of what the boards believe are the rights sold in the respective scenarios. This could be accomplished either through an amendment to the principle or illustrative examples within the guidance.

We further recommend that the boards complete a reconsideration of this guidance and a comparison to the conclusions reached within the Leasing Exposure Draft to ensure there is a consistent principle or there are appropriate differences between the models that warrant the alternative approaches.

Question 17

The boards propose that in accounting for the gain or loss on the sale of some non-financial assets (for example, intangible assets and property, plant and equipment), an entity should apply the recognition and measurement principles of the proposed revenue model. Do you agree? If not, why?

We believe that after the boards address the issues raised by this and other comment letters, a final standard should provide appropriate revenue recognition guidance. We agree that the recognition and measurement principles of a final revenue standard would be suitable for consideration in the determination of gains and losses on the sale of some non-financial assets. We believe such guidance should apply when there is no other existing GAAP. In that regard, the boards should also address the interaction of the final revenue standard with other guidance such as the guidance for non-monetary exchanges, derecognition (including derecognition due to deconsolidation of a subsidiary that represents an in-substance non-financial asset, for example, in-substance real estate such as the EITF is currently considering in EITF Issue No. 10-E, *Deconsolidation of a Subsidiary That Is In-Substance Real Estate*), transfers, contributions, etc. We further believe that it would not be appropriate for this standard to address presentation or disclosure requirements for transactions involving the sale of non-financial assets.

Question 18

[FASB only] Should any of the proposed requirements be different for non-public entities (private companies and not-for-profit organisations)? If so, which requirement(s) and why?

One of the Exposure Draft's key objectives is to enhance guidance by establishing "principles that an entity shall apply to report useful information to the users of its financial statements about the amount, timing and uncertainty of revenue and cash flows arising from a contract with a customer." We do not believe this principle changes whether one is a public or non-public entity. An accurate portrayal of a company's revenue is critical to the depiction of the overall health of an entity. We therefore do not support any proposal which suggests a differing recognition and measurement model for the recognition of revenue on the basis of whether that entity is public or non-public.

We do believe, however, that the extensive financial statement disclosures represent a prohibitive effort and cost to non-public entities. We support an overall reduction in the required disclosures as suggested within our response to Question 10. For non-public entities, we generally support the proposed qualitative disclosures but believe the quantitative disclosures are excessive and prohibitively costly. We therefore suggest disclosure relief for non-public entities from the requirements in paragraphs 73a & b, 74, 75, 78 and 80 due to cost/benefit and financial statement user needs considerations.

The boards should also consider clarifying that government regulators charged with the market oversight for a particular jurisdiction will generally determine which entities are considered "non-public" for purposes of applying this and other standards.

We also believe that, for a variety of practical reasons, sufficient additional time should be provided to permit non-public companies to adopt the standard. We suggest an additional two-year transition period would be appropriate for non-public companies.