

October 2, 2015

Ms. Susan M. Cospers  
Technical Director  
Financial Accounting Standards Board  
401 Merritt 7  
PO Box 5116  
Norwalk, CT 06856-5116

**File Reference No. 2015-290**

Dear Ms. Cospers:

McGladrey LLP is pleased to comment on the Proposed Accounting Standards Update (ASU), *Revenue from Contracts with Customers (Topic 606): Principal versus Agent Considerations (Reporting Revenue Gross versus Net)* (the "proposed ASU"). Overall, we are very supportive of the actions the Board has taken to address questions and issues arising in the implementation of the new revenue recognition model provided in ASU 2014-09, *Revenue from Contracts with Customers (Topic 606)*. The work of the Joint Transition Resource Group for Revenue Recognition (TRG) has been very valuable in understanding how certain aspects of ASC 606 should be applied in practice and in identifying those issues that warrant additional standard setting by the Board. The TRG's discussions and the Board's additional standard setting will significantly enhance comparability between reporting entities as the new revenue recognition model is implemented.

As it relates to the principal versus agent considerations addressed in the proposed ASU, we are supportive of the Board's efforts to improve the operability and understandability of the principal versus agent guidance in ASC 606 and believe that the Board's proposals make significant strides in this direction. Provided below for your consideration are our responses to the "Questions for Respondents" on which specific comment was requested. In our responses to these questions, we highlight additional clarifications that we believe would further improve the operability and understandability of the principal versus agent guidance in ASC 606.

**Responses to Questions for Respondents**

**Question 1:** *The proposed amendments to paragraph 606-10-55-36 clarify the unit of account (the "specified good or service") at which an entity would determine whether it is a principal or an agent and clarify that an entity can be both a principal and an agent in a single contract. Would the proposed amendments improve the operability and understandability of the principal versus agent guidance in Topic 606? If not, please explain why and suggest alternatives.*

We believe the proposed amendments accomplish the objective of clarifying the unit of account to which the principal versus agent guidance in ASC 606 should be applied and that the entity can be both a principal and an agent in a single contract. Although, we believe consideration should be given to further clarifying the unit of account in the context of the broader revenue recognition model in ASC 606 by explaining the relationship between "specified good or service" and "performance obligation" given the similarities in their definitions (i.e., distinct good or service or distinct bundle of goods and (or) services). This could be accomplished by bringing some of the discussion in paragraph BC13 into ASC 606-10-55-36.

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**Question 2:** *Paragraph 606-10-55-37A clarifies application of the control principle to certain types of arrangements by explaining what a principal controls before the specified good or service is transferred to the customer. Would the proposed amendments improve the operability and understandability of the principal versus agent guidance in Topic 606? If not, please explain why and suggest alternatives.*

We believe the proposed amendments clarify application of the control principle to the specified good or service, particularly through application in the examples. However, we also believe the proposed amendments raise a question about how to determine whether an analysis of the control principle is conclusive such that the indicators in ASC 606-10-55-39 do not need to be evaluated. An explicit conclusion is reached in Example 46 that the indicators do not need to be considered because evaluation of the control principle was conclusive. By virtue of the fact that the indicators were applied, the implicit conclusions reached in the other examples were that the evaluations of the control principle were not conclusive. We believe it is critical for an explanation to be provided in each of the examples about why evaluation of the control principle was either conclusive or not conclusive. Without this explanation, we believe consistent application of the control principle and indicators is very unlikely. Given the principal versus agent guidance that exists in current U.S. generally accepted accounting principles (and its sole reliance on an indicator model) and the frame of reference that constituents are coming from as a result, we believe clear explanation must be provided related to how the indicators in ASC 606-10-55-39 supplement the control principle evaluation.

We believe certain of the concepts in paragraph BC24 should be incorporated in ASC 606-10-55-37A(b) to provide additional context around how an entity determines whether it controls the right to a service being sold to a customer. Specifically, the concepts related to it often being “relevant to assess whether the right is created only when it is obtained by the customer, or whether the right to goods or services exists before the customer obtains the right. If the right does not exist before the customer obtains it, an entity (that is an intermediary) would be unable to control that right before it is transferred to the customer.” Regardless of whether these concepts are left in paragraph BC24 or incorporated in ASC 606-10-55-37A(b), we believe it would also be helpful to explain why the concepts are or are not relevant in the context of Example 46A given that the entity only engages the third-party service provider in that example after it enters into a contract with a customer, but the conclusion is reached that the entity is a principal in the transaction with the customer.

**Question 3:** *The proposed amendments to paragraph 606-10-55-39 provide indicators of when an entity controls the specified good or service before it is transferred to the customer and, therefore, would be a principal. The amendments also clarify the relationship of each indicator to the control principle in paragraph 606-10-55-37. Paragraph 606-10-55-39A was added to explain that the indicators may be more or less relevant to the principal versus agent assessment depending on the nature of the arrangement and that different indicators may provide more or less persuasive evidence about whether the entity controls the specified good or service before it is transferred to the customer in different contracts. Would the proposed amendments improve the operability and understandability of the principal versus agent guidance in Topic 606? If not, please explain why and suggest alternatives.*

We believe the proposed amendments to ASC 606-10-55-39 and the addition of ASC 606-10-55-39A improve the operability and understandability of the principal versus agent guidance in ASC 606. However, as explained further in our response to Question 2, we believe additional amendments are necessary to further explain how the indicators in ASC 606-10-55-39 supplement the control principle. While the new discussion in ASC 606-10-55-39A is helpful by indicating that the indicators only play a supporting role to the control principle and there is no recipe for how they should be applied, it does not provide enough direction on when they should be applied (i.e., when is evaluation of the control principle conclusive) and how to determine when an indicator is relevant in one situation, but not in another situation. Given that any additional direction provided in this area is based heavily on facts and

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circumstances, the best place for such direction is likely in the examples. As discussed in our response to Question 4, we believe each of the examples should explain if (and why) the evaluation of the control principle is conclusive or not, and if evaluation of the control principle is not conclusive, which indicators are relevant (and why).

We also believe the intent of the discussion in ASC 606-10-55-39A, as well as the indicators themselves, could be further bolstered by bringing in some of the incremental observations in BC15, including the following: (a) the indicators do not override the assessment of control and (b) do not constitute a separate or additional evaluation.

In addition, we believe the following observations should be made in ASC 606-10-55-39:

- Indicators (a) and (b) are typically more relevant in the principal versus agent analysis. While some constituents may infer that from the caveats added to indicators (c) and (e) (i.e., the sentences beginning with “However”), other constituents may not. Given that indicators (a) and (b) are typically more relevant, we believe an explicit statement to that effect will foster consistent application of the guidance.
- Less inventory risk exists in a situation with back-to-back return rights (i.e., if the customer returns goods to the entity, the entity can return the goods to its supplier). The observation could be made in indicator (b) or illustrated in an additional example.

**Question 4:** *Would the revisions to the principal versus agent illustrative examples (Examples 45 through 48) and the added illustrative examples (Examples 46A and 48A) improve the operability and understandability of the principal versus agent guidance in Topic 606? If not, please explain why and suggest alternatives.*

We believe the revised and new examples improve the operability and understandability of the principal versus agent guidance in ASC 606. However, as explained further in our response to Question 2, we believe additional analysis should be provided in the examples to explain why evaluation of the control principle was or was not conclusive without considering the indicators in ASC 606-10-55-39. Providing this analysis will help constituents understand when they need to move beyond just the control principle itself to the indicators. In addition, while we understand and appreciate the new discussion in ASC 606-10-55-39A and BC15, we believe additional explanation should be provided in the examples regarding why indicators are deemed relevant (or not relevant) to the analysis. For instance, in Example 47 (ASC 606-10-55-328C), indicator (a) was not analyzed. Given that indicator (a) is focused on who is “primarily responsible,” we would have thought it should be analyzed in this (and virtually all) fact patterns in which the indicators are analyzed. When it comes to the indicators, we believe the first step in the principal versus agent guidance in ASC 606 is to analyze and explain why an indicator is relevant or not relevant and the second step is to analyze those indicators that are relevant to determine whether they point to the entity being a principal or an agent. While a conclusion on the first step is inherently reached in each example, the basis for that conclusion is not provided in all the examples. Without providing an explicit explanation in each of the examples regarding why an indicator was deemed relevant or not relevant, we question whether enough guidance has been provided to facilitate consistent conclusions on the relevance of the indicators in similar facts and circumstances. In addition, only focusing on certain indicators in an example may give the impression that the intent of the analysis is to look for confirming evidence and not disconfirming evidence.

In addition, we believe the following revisions also need to be made to the examples:

- ASC 606-10-55-318C(a): Change the perspective of the analysis to why the entity *is not* primarily responsible for fulfilling the promise to the customer instead of why the supplier *is* primarily responsible to be consistent with the indicator in ASC 606-10-55-39(a).

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- ASC 606-10-55-319: Either remove “(which, in this example, is when goods are purchased by the customer)” (given that the focus of the example is principal versus agent determination and not when performance obligations are satisfied) or explain why, in the context of Step 5, the entity satisfies its performance obligation to arrange for the goods to be provided by the supplier to the customer when the customer purchases the goods (in contrast to when the goods are shipped).

We appreciate this opportunity to provide feedback on the proposed ASU and would be pleased to respond to any questions the Board or its staff may have concerning our comments. Please direct any questions to Rick Day at 563.888.4017 or Brian H. Marshall at 203.312.9329.

Sincerely,

A handwritten signature in cursive script that reads "McGladrey LLP".

McGladrey LLP