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2015-290  
Comment Letter No. 12  
330 North Wabash, Suite 3200  
Chicago, IL 60611

October 15, 2015

Via email to [director@fasb.org](mailto:director@fasb.org)

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

Re: Revenue from Contracts with Customers (Topic 606): Principal versus Agent Considerations (File Reference No. 2015-290) ("the ED")

Dear Ms. Cospers:

We are pleased to provide comments on the Board's proposed clarifications to the principal versus agent guidance. That assessment often involves substantial judgment, which may lead to diversity in practice. As such, we support the Board's objective to clarify the principal versus agent guidance in the context of the control principle in Topic 606.

Toward that end, we have several suggestions for improving the final amendments. As drafted, they rely heavily on the basis for conclusions. We believe there are important concepts that should be elevated from the basis into the final amendments to the Codification, such that the amendments stand on their own. These points are included in our responses to the Board's specific questions in the Appendix to this letter.

We would be pleased to discuss our comments with the FASB staff. Please direct questions to Adam Brown at (214) 665-0673 or Ken Gee at (415) 490-3230.

Very truly yours,

A handwritten signature in black ink that reads "BDO USA, LLP". The letters are written in a cursive, slightly slanted style.

BDO USA, LLP

## Appendix

**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 generally agree that the proposed amendments would clarify the thought process to be applied when assessing whether an entity is a principal or an agent. The entity should determine the nature of the promise in a two-step sequence: (1) identify the specified good or service, and (2) assess whether it controls that good or service, i.e., if the entity controls the specified good or service, it is the provider of that good or service and therefore it is a principal and not an agent. Establishing this framework should promote greater consistency in applying the principal versus agent guidance.

However, we note the amendments are drafted primarily from the entity’s perspective for purposes of this control assessment. It is unclear whether entities can or should consider the customer’s perspective to determine whether revenue should be presented gross or net. The Board has previously stated:

...the assessment of when control has transferred could be applied from the perspective of either the entity selling the good or service or the customer purchasing the good or service. Consequently, revenue could be recognized when the seller surrenders control of a good or service or when the customer obtains control of that good or service. Although in many cases both perspectives lead to the same result, *the Boards decided that control should be assessed primarily from the perspective of the customer*. That perspective minimizes the risk of an entity recognizing revenue from undertaking activities that do not coincide with the transfer of goods or services to the customer.<sup>1</sup>

While the preceding language focuses on the recognition of revenue, some stakeholders may believe a customer perspective similarly informs the presentation of revenue. Example 45 discusses an entity that operates a retail website to facilitate sales from suppliers to customers, who remit payment on the website. In that example, the reporting entity observes that its website is a marketplace for buyers and sellers; however, the customer may view the retailer as the seller of the good or service. The customer may have that perspective for several reasons, including the fact that the transaction was not possible without the website and payment was required through the website. Indeed, the customer may not even be aware that the entity lacks control of the good or service.

If the Board does not intend for the customer’s perspective to be a factor in determining the specified good or service under 606-10-55-36 through 55-40, we recommend clarifying this. While the amendment in paragraph 55-38 clearly states an entity is an agent when it does not control the specified good or service, the standard would be more operational by stating this analysis is made only from the reporting entity’s perspective.

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<sup>1</sup> BC121, ASU 2014-09, *Revenue from Contracts with Customers*

**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 can be improved by elevating key concepts from the basis for conclusions into the authoritative text. These changes would help clarify how to apply the control principle to services. Therefore, we recommend incorporating language from BC24 into 606-10-55-37A(b), as follows (added text is underlined):

When another party is involved in providing goods or services to a customer, an entity that is a principal obtains control of:

- b. A right to a service to be performed by the other party, which gives the entity the ability to direct that party to provide the service to the customer on the entity's behalf. In doing so, it is often 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.

The underlined language requires a focus on when the right to a service originates. We believe including express guidance on how to determine that the entity has control of a right by evaluating when the right arises will make the amendments more operational. In contrast, simply alluding to when a right originates in the proposed amendments by virtue of the entity's ability to redirect the right is less clear.

Adding this language will also provide context for Examples 46A and 47. In Example 46A, the reporting entity has the ability to direct the service provider to provide services on the entity's behalf, and the entity concludes that it obtains control of the right to those services before they are provided to the customer.<sup>2</sup> Similarly, Example 47 states that an entity has inventory risk with respect to airline tickets "because the entity committed to obtain the tickets from the airlines before obtaining the contract with a customer to purchase the tickets."<sup>3</sup> Since both examples rely on the concept of timing, the standard would be improved by more clearly articulating the notion of timing in paragraph 55-37A(b).

Further, with respect to inventory risk, the language in paragraph 606-10-55-39(b) appears to equate actually obtaining a right to a service with a commitment to obtain the right, as follows (italics added):

Indicators that an entity controls the specified good or service before it is transferred to the customer include, but are not limited to, the following:

- b. The entity has inventory risk before the specified good or service has been transferred to a customer, or after that transfer (for example, on return). For

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<sup>2</sup> 606-10-55-324E

<sup>3</sup> 606-10-55-328C

example, *if the entity obtains, or commits to obtain*, the specified good or service before obtaining a contract with a customer, that may indicate that the entity has the ability to direct the use of, and obtain substantially all of the remaining benefits from, the good or service before it is transferred to the customer.

If an entity obtains a right to service prior to obtaining a contract with a customer, the entity is still presumably obligated to compensate the service provider, which would indicate the entity may be a principal. However, a commitment to obtain a service may be contingent on obtaining a customer contract, in which case the entity's principal vs. agent status is less clear because payment to the service provider is also contingent. As such, we recommend rephrasing paragraph 55-37A(b) as follows (added text is underlined):

- b. The entity has inventory risk before the specified good or service has been transferred to a customer, or after that transfer (for example, on return). For example, if the entity obtains, or commits to obtain, the specified good or service before obtaining a contract with a customer and is obligated to compensate the vendor, that may indicate that the entity has the ability to direct the use of, and obtain substantially all of the remaining benefits from, the good or service before it is transferred to the customer.

These revisions would be consistent with two contrasting examples in the ED. In Example 46A, an entity that outsources the provision of office maintenance services concludes it lacks inventory risk because it does not contract with a third party service provider until after obtaining a contract with a customer.<sup>4</sup> Example 47 addresses a reseller of airline tickets and indicates "the entity agrees to buy a specific number of tickets and must pay for those tickets regardless of whether it is able to resell them..."<sup>5</sup> The entity has inventory risk with respect to the tickets because the entity committed to obtain the tickets from the airlines before obtaining the contract with a customer to purchase the tickets."<sup>6</sup>

Lastly, we suggest the following edits to paragraph 606-10-55-37A to clarify that each scenario is independent of the other two (added text is underlined):

When another party is involved in providing goods or services to a customer, an entity that is a principal obtains control of:

- a. A good or another asset from the other party that it then transfers to the customer<sub>;</sub>
- b. A right to a service to be performed by the other party, which gives the entity the ability to direct that party to provide the service to the customer on the entity's behalf<sub>;</sub> or
- c. A good or service from the other party that it then combines with other goods or services in providing the specified good or service to the customer. If an entity provides a significant service of integrating goods or services provided by another party into the specified good or service for which the customer has contracted, it controls the specified good or service before that good or service is transferred to the customer. In that case, the entity first obtains control of

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<sup>4</sup> 606-10-55-324F

<sup>5</sup> 606-10-55-325

<sup>6</sup> 606-10-55-328C

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the good or service from the other party and directs its use to create the combined output that is the specified good or service.

**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 support the flexibility that the standard offers in applying the control indicators guidance and since it does not prescribe weighting, we believe that it will facilitate practitioners' use of judgment. However, in paragraph 606-10-55-39A, we recommend the following addition, based on the guidance in BC21 of the basis for conclusions that clarifies the two sets of factors are intended for different purposes, i.e., they distinguish between i) whether and ii) when customer obtains control of a promised good or service (added text is underlined):

The indicators in paragraph 606-10-55-39 may be more or less relevant to the assessment of control depending on the nature of the specified good or service and the terms and conditions of the contract. In addition, different indicators may provide more persuasive evidence in different contracts. However, the indicators in paragraph 606-10-25-30 shall not be considered for purposes of the principal versus agent evaluation in paragraphs 606-10-55-36 through 55-40.

In addition, please see our response to Question 2 for additional recommendations to enhance the principal vs. agent indicators.

**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 generally agree that the illustrative examples help in applying the principal versus agent guidance. However, we recommend providing at least one example where more than one control indicator conflicts with the control conclusion. An example would illustrate the statement added to paragraph 606-10-55-38: "An entity that is an agent does not control the specified good or service provided by another party before that good or service is transferred to the customer."

For instance, consider an example in which an entity resells off-the-shelf software and provides services to its customers. While the entity does not take control or possession of the software (or a right to the software) prior to obtaining a contract with a customer, the entity bears the credit risk on collecting the consideration for the software and the services. The entity also sets the software price to the end customer. In this scenario, the amendments in paragraph 55-38 would

preclude presenting the revenue associated with the software on a gross basis, despite the fact that the entity has latitude to establish pricing and also bears credit risk.

Separately, as an editorial matter, certain clarifications to Examples 47 and 48 may be warranted. The examples address the provision of airline tickets and restaurant vouchers, respectively. Each example includes a statement that besides these promised goods or services, “the entity observes that no other promises are made to the customer.”<sup>7</sup> However, in both examples, the entity also assists customers with resolving complaints that are directed to third party provider (i.e., the airline and the restaurant). We recommend clarifying that assisting with complaint resolution is considered immaterial in the context of the contract to support the conclusions in each example that there are no other promises to evaluate for purposes of the gross vs. net presentation.

In addition, we suggest the following clarifications to paragraph BC26 and BC36 (added text is underlined, deleted text is ~~struck out~~):

BC26. When a specified good or service is a distinct bundle of goods or services, the principal versus agent analysis may, in some cases, be straightforward. The Boards concluded (in paragraph 606-10-55-37A(c)) that when an entity provides the significant service of integrating two or more goods or services into the combined output that is the specified good or service for which the customer contracted, it controls that specified good or service before it is transferred to the customer. The entity also controls the goods or services provided by the other party that are inputs to the specified good or service by directing their use to create the combined item. In that case, the inputs provided by the other party would be a fulfilment cost to the entity. In contrast, if a third party provides the significant integration service, then the entity’s customer for its goods or services (which would be inputs to the specified good or service) is likely the other that third party.

BC36. The Board’s view is that on the basis of the transaction price guidance in Section 606-10-32, the transaction price of a principal does not include the difference between the amount to which an entity is entitled from the intermediary and the amount charged by the intermediary to an end customer when the entity is (and expects to remain)...

The parenthetical phrase “(and expects to remain)” may raise questions as to whether it suggests that an ongoing assessment is needed. Further, we suggest that the Board clarify whether its conclusion would be different if the entity does not expect to remain unaware of the amount the intermediary charged to the end customer.

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<sup>7</sup> 606-10-55-327 and 606-10-55-328A