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October 15, 2015

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

**File Reference No. 2015-290**

**Re: Proposed Accounting Standards Update, *Principal Versus Agent Considerations (Reporting Revenue Gross Versus Net)***

Dear Ms. Cospier:

Deloitte & Touche LLP appreciates the opportunity to comment on the FASB's proposed Accounting Standards Update (ASU) *Principal Versus Agent Considerations (Reporting Revenue Gross Versus Net)*.

We support the Board's efforts to clarify and improve ASC 606 to help reduce potential diversity in practice and the initial and ongoing costs of applying the new revenue standard. We believe the amendments in the proposed ASU are necessary to ensure that ASC 606 is understood and practical to implement. Further, we encourage the FASB to continue its convergence dialogue with the IASB as these and other amendments to ASC 606 move forward.

We support the Board's proposed amendments to the guidance on determining whether an entity's obligation is to provide a good or service to a customer (i.e., the entity is a principal) or to arrange for a third party to provide that good or service (i.e., the entity is an agent). In particular, we support the proposed amendments that clarify:

- The need to identify the specified goods or services in the contract, including rights to goods or services provided by another entity.
- That a principal is the party who controls the specified goods or services before those goods or services are transferred to the customer.
- How the use of the control model in the principal-versus-agent assessment is correlated with the application of the control model under other guidance in ASC 606.

While we believe that these proposed amendments would be beneficial to the practical application of ASC 606, we recommend that the Board reframe the guidance in ASC 606-10-55-39 to make certain indicators determinative of control. Much of the difficulty in current practice is that current guidance for determining whether to present revenue gross or net contains numerous indicators without a clear framework for making judgments when several indicators point towards contrary directions.

In addition, the proposed amendments address and catalogue the delivery of goods and services separate from rights to goods and services provided by a third party. We recommend that the Board include guidance differentiating how an entity assesses control when the specified goods or services are actual goods and services as compared to rights to goods or services.

Specifically, we believe that when the specified good or service is the actual good or service the customer receives (i.e., not just a right to acquire the good or service from a third party), the characteristics in ASC 606-10-55-39(a) and aspects of 55-39(b) — which discuss whether an entity is primarily responsible for fulfillment of the specified goods and services and the part about whether the entity has inventory risk *before* the good or service is transferred to the customer, respectively — are determinative of whether the entity controls the specified good or service before it is transferred to the customer. Therefore, if an entity possesses either of these characteristics, it is the principal in the transfer of the goods or services to the customer. However, because inventory risk is not always applicable for either party and an entity must often use judgment in evaluating whether it is primarily responsible for fulfilling the promise to provide a good or service, as discussed in our response to question 3 herein, we believe that the Board should include additional guidance in the final ASU that helps an entity exercise the judgment necessary to determine who is primarily responsible.

Conversely, when the specified good or service is a right to a good or service to be provided by another entity, the assessment of whether the entity is primarily responsible for fulfillment is not applicable (i.e., as the entity is providing a *right* to a third party's good or service and not the good or service itself, the entity is never primarily responsible for providing the underlying good or service). Therefore, we believe that the characteristic in ASC 606-10-55-39(b) should be determinative and needs to be present for an entity to conclude that it controls the right to the good or service before it is transferred to the customer.

As currently proposed, the ASU provides indicators without a framework for how the indicators interact and without sufficient clarity on how judgements should be made. Although ASC 606-10-55-39A notes that the indicators may be more or less relevant to the principal-versus-agent assessment depending on the nature of the arrangement, we believe that an entity applying the proposed guidance, as currently drafted, may give each indicator equal relevance or over-emphasize weaker indicators. Therefore, if certain indicators are not designated as determinative, an entity may draw an inconsistent conclusion by placing too much reliance on other indicators, such as credit risk and pricing discretion. This could perpetuate the diversity that currently exists.

With respect to determining the transaction price as a principal, it is unclear how an entity would account for situations in which there is a difference between the amount to which the entity is entitled from the intermediary and the amount charged by the intermediary to an end customer. We note that paragraphs BC36–BC38 of the proposed ASU's Basis for Conclusions indicate that a principal does not include in the transaction price “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) unaware of the amount that the intermediary charged to the end customer.” We recommend that the Board move the guidance in these paragraphs into the final standard rather than the basis for conclusion. Further, we believe that the Board should clarify the guidance to address such differences for situations in which the entity is aware of the amount charged by the intermediary to the end customer.

We also understand that the Board is aware that questions about whether an entity is a principal or an agent under the existing revenue guidance in ASC 605-45 are presently among the most common reasons for consultations between entities and regulators and between entities and their auditors. To alleviate current practice issues related to applying the principal-versus-agent guidance, we encourage the Board to consider

File Reference No. 2015-290  
October 15, 2015  
Page 3

whether improvements similar to those in the proposed ASU, and recommended herein, should be made to existing U.S. GAAP (i.e., effective sooner than effective date for ASC 606).

We believe that transition resources such as the FASB-IASB joint revenue recognition transition resource group and AICPA industry task forces have been an integral part of the implementation process and will remain so. We strongly support the FASB's efforts to monitor entities' implementation progress, publicly address implementation questions, assist entities and auditors during transition, and continue the dialogue with the IASB.

We will continue to work closely with our clients throughout their implementation process. However, a successful audit of the application of the new standard is directly linked to the readiness of our clients. Accordingly, we encourage the FASB to continue its outreach with financial statement preparers to understand their implementation status and progression toward successful transition.

The appendix below contains our responses to the proposed ASU's questions for respondents.

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We appreciate the opportunity to comment on the proposed ASU. If you have any questions concerning our comments, please feel free to contact Mark Crowley at (203) 563-2518.

Yours truly,

Deloitte & Touche LLP

cc: IASB: Hans Hoogervorst, Chairman; Ian Mackintosh, Vice-Chairman  
Robert Uhl  
Eric Knachel  
Veronica Poole  
Phil Barden

**Appendix**  
**Deloitte & Touche LLP**  
**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.*

Yes, we believe that the proposed amendments that clarify the unit of account for applying the principal-versus-agent guidance and that an entity can be both a principal and an agent in a single contract will improve the operability and understandability of the guidance.

*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.*

Yes, we believe that the proposed amendments generally improve the operability and understandability of the principal-versus-agent guidance in ASC 606. However, we believe that the Board should clarify whether an entity’s assessment under ASC 606-10-55-37A(c) should be consistent with its identification of performance obligations under ASC 606-10-25-21(a). Further, under the proposed ASU, it appears that an entity would not need to consider the indicators in ASC 606-10-55-39 (to determine whether it controls the goods or services before they are transferred to the customer) if the entity meets the criterion in ASC 606-10-55-37A(c). Specifically, if the entity provides a service of significant integration (i.e., integrating a good or service provided by another party into the specified good or service), the entity would (1) conclude that it controls the goods or services before they are transferred to the customer and (2) not need to evaluate either whether it has inventory risk or whether it is the party primarily responsible for fulfilling the promise(s) to the customer. In other words, the guidance in ASC 606-10-55-37A(c) is determinative of whether an entity controls the specified good or service and therefore is the principal. Because concluding an entity provides a significant service of integrating a good or service with other goods or service will often require judgment when a good or service is provided by another party, we believe evaluating the criteria/indicators in ASC 606-10-55-39 would be useful in determining whether an entity controls the goods or services before they are transferred to the customer. Additionally, we believe the Board should clarify whether it intended to narrowly define the concept in 606-10-37A(c) only to those circumstances that meet 606-10-25-21(a) or to any of the attributes of separately identifiable in all of 606-10-25-21.

*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 agree that the proposed amendment in ASC 606-10-55-39 would help clarify the relationship of each indicator to the control principle in ASC 606-10-55-37; however, we do not agree with how the indicators are characterized. The amendments do not change the fact that none of the indicators are weighted in terms of

relative importance to the principal-versus-agent assessment. In other words, none of the indicators are determinative of whether an entity is acting as a principal (or conversely as an agent). We believe that certain proposed indicators are determinative of control, while others, at most, should be evaluated as secondary characteristics (indicators) that support an entity's judgments in performing the assessment. As a result, although ASC 606-10-55-39A notes that the indicators may be more or less relevant to the principal-versus-agent assessment depending on the nature of the arrangement, we believe that an entity applying the guidance may give each indicator equal relevance and therefore may draw an incorrect or inconsistent conclusion. Further, because none of the indicators are designated as determinative, diversity in practice may result because entities may interpret the importance of each indicator differently. In addition, we believe that the indicators (criteria) should be evaluated differently depending on whether the entity's promise is to transfer a good or service itself or to transfer a right to a good or service to be provided by another party.

When the specified good or service is the actual good or service (rather than a right), we believe that the characteristics described in ASC 606-10-55-39(a) and aspects of 55-39(b) are determinative of control. Specifically, if an entity is primarily responsible for fulfilling its promise to provide a good or service or the entity has inventory risk *before* the specified good or service has been transferred to the customer, it is a principal. However, we note that inventory risk may not be present in certain arrangements, specifically those involving the sale of virtual goods or services, and we believe that an entity will need to use judgment when determining whether it is primarily responsible for providing the good or service. Additionally, the presence of inventory risk after the transfer of the good or service to the customer (for example, on return) may not be determinative of control, but may assist in determining which party is primarily responsible for the acceptability of the specified good or service. Therefore, the Board should consider identifying this and other secondary indicators to help entities use judgment in such situations. For example, we believe an entity that is primarily responsible for fulfilling its promise to provide the specified good or service to a customer will often have discretion in establishing the price charged to the customer (as currently described in ASC 606-10-55-39(c)) or in selecting a third-party supplier or service provider. Accordingly, we recommend that the Board include these as indicators that an entity is primarily responsible for providing the goods or services to the customer; however, the Board should note that the presence of these indicators would not, in isolation, be determinative of whether an entity controls the goods or services before they are transferred to the customer.

When the specified good or service is a right to a good or service to be provided by another entity, we believe that only the characteristic described in ASC 606-10-55-39(b), that is inventory risk, is determinative of control and would need to be present to conclude that the entity controls the right to the good or service before it is transferred to the customer. Therefore, if an entity has inventory risk with respect to a right to a good or service, it is a principal.

Further, the proposed additional guidance in ASC 606-10-55-39(d) correctly notes that an agent may choose to accept credit risk; we do not believe that the existence of credit risk should affect an entity's assessment of whether it is a principal or an agent in the arrangement. We also note that (1) customer credit risk is identified in current U.S. GAAP (ASC 605-45-45-13) as a weak indicator that an entity is a principal and (2) in practice, this indicator is rarely, if ever, persuasive evidence. Therefore, we recommend that the Board remove ASC 606-10-55-39(d) from the final ASU because it is not helpful in determining whether an entity controls a specified good or service.

We also suggest that the Board make other minor modifications to the wording in ASC 606-10-55-39(b). Specifically, we believe that the intent of stating that an entity has inventory risk *after* the specified good or service is transferred to the customer is related to situations in which the customer has a general right of return. This concept is currently explained in ASC 605-45-45-5, which states that an entity has general inventory risk if it "will take title to the product if it is returned by the customer (that is, back-end inventory risk) **and the**

**customer has a right of return**” (emphasis added). We believe that the ASU should clarify this point to avoid unintended consequences in which an entity determines that it has inventory risk because the customer may return a good as a result of a defect or other warranty issues.

*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.*

Yes, the revisions to the illustrative examples would help improve the operability of principal-versus-agent guidance. However, as discussed below, we have several observations and suggestions about certain of the illustrative examples.

Example 46 indicates that the entity controls the specified good or service — specialized equipment in the example — because the entity provides the significant integration service necessary to produce the specialized equipment. This conclusion appears to be based on the fact that the entity is responsible for the overall management of the contract and therefore “provides a significant service of integrating those items into the combined output — the specialized equipment.” However, it is not clear what factors led to the conclusion that the entity provides the significant integration service to produce the specialized equipment. Further, some of the factors the example cites to support the conclusion that the entity controls the specialized equipment before that equipment is transferred to the customer could also be applicable if the entity concludes that its obligation is to arrange for the third party to supply the specialized equipment to the customer (i.e., the entity is an agent). Specifically, the third party might not be able to direct the equipment to another party once the entity, as an agent, arranges for the third party to manufacture the equipment for the customer. The agent may also accept credit risk as part of its obligation to arrange for the third party to deliver the specialized equipment to the customer, thereby entitling the agent to the consideration in the contract from the customer. We recommend that the Board clarify the reason(s) that led to the conclusion that the entity provides a significant integration service pursuant to ASC 606-10-25-21(a). We also believe the example should include an evaluation of the criteria/indicators in ASC 606-10-55-39.

Similarly, Example 48A illustrates a contract in which an entity concludes that it is a principal with respect to the recruitment services but is an agent with respect to the third party’s database service. A critical assumption in reaching these conclusions is the fact that the recruitment services and the database access are distinct. It would seem that if the entity concludes that it has provided a significant service of integrating the recruiting services and the database access into the specified service for which the customer has contracted, the conclusion reached in the example may be different. That is, the entity may have concluded that it controls the database by applying the guidance in ASC 606-10-55-37A(c). Therefore, given the importance of determining whether the services are distinct, the Board should clarify the reason(s) that led to the conclusion that the entity does not provide a significant integration service pursuant to ASC 606-10-25-21(a).

Examples 47 and 48 both deal with situations in which the specified good or service is a right to a service to be performed by another entity. In Example 47, the entity concludes that it controls the specified good or service and therefore is a principal, while in Example 48 the entity concludes that it does not control the specified good or service and therefore is an agent. It appears that the primary reason for the difference between these conclusions is that in Example 47, the entity has inventory risk whereas in Example 48 it does not. This seems to imply that the presence of inventory risk is determinative of control in situations in which the specified good or service is a right to a service. In those situations, it would seem unlikely that an entity would determine that it is primarily responsible for transferring the underlying good or service provided by the other entity; rather, the entity would conclude that it is primarily responsible for transferring the right to the underlying service. In

File Reference No. 2015-290  
October 15, 2015  
Page 7

these situations, we do not believe the entity could transfer a right to the good or service as a principal unless it controlled the right (i.e., had inventory risk) before the right was transferred to the customer. Therefore, we believe the Board should clarify that the inventory risk indicator is determinative of control, as we suggest in our response to Question 3.