



3979 Freedom Circle, Suite 700  
Santa Clara, CA 95054

P: (650) 251 0074  
F: (650) 396 8071

November 22, 2015

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

File Reference No. 2015-320

Dear Ms. Cospers:

Connor Group, Inc. is pleased to provide our comments on the Proposed Accounting Standards Update, Revenue from Contracts with Customers (Topic 606), Narrow-Scope Improvements and Practical Expedients. Connor Group was founded in 2005 and is a technical accounting advisory firm built of Big 4 alumni and industry executives. We currently have over 400 clients and specialize in helping our clients solve complex technical accounting issues under both US GAAP and IFRS, with revenue recognition being a heavy focus area. Our clients represent industries such as technology, software, Internet, cloud services, life sciences and manufacturing, amongst others. In addition, we assist many of our clients with aspects of their accounting and financial reporting during their IPO filing process.

Because our concerns regarding requirements for collectibility assessment are broader in scope than the questions formulated by the Board and cross the lines between the various paragraphs in ASC 606 where collectibility is addressed, we have provided our views on this topic immediately below. We have responded to the questions asked by the Board following this section.

### ***Improvements in Assessing Collectibility***

#### Improvements Proposed by the Board

We strongly support the Board's intention to provide narrow-scope improvements and practical expedients to Topic 606. Further, we do believe that the proposed amendments improve the application of collectibility threshold for certain customer contracts. For example, in the case of a contract that provides for collection of royalty from a customer at the point where there are no remaining performance obligations, under the new paragraph 606-10-25-7(c) the entity would be able to recognize revenue upon collection of royalty, presuming such amounts are nonrefundable. Similarly, in the case of a typical customer contract for a semi-conductor entity under which, following grant of an initial license, the entity ships to the customer microchip products for which a fixed fee is due, and in addition the customer must pay royalty for each product containing the entity's microchip that is sold during a multi-year term of the contract, paragraphs 606-10-55-3B and 3C adequately clarify that the assessment can be limited to just those items which the entity is willing to supply to the customer prior to potentially stopping the supply in the event the customer does not pay the consideration when it is due. We would like to highlight that in our mind, the words "will be transferred to the customer" in paragraph 606-10-25-1(e) are potentially



Exposure Draft: Proposed Accounting Standards Update, Revenue from Contracts with Customers (Topic 606), Narrow-Scope Improvements and Practical Expedients  
November 22, 2015  
Page 2

ambiguous and confusing, because, without the background, they are more likely to be read to refer to the full contractual obligations of the entity, as opposed to the quantities the entity is willing to supply to the customer prior to being paid.

*Examples of Collectibility Assessment That Still Cause Issues*

However, we believe the proposed enhancements to paragraphs 606-10-55-3A through 3C and 606-10-25-7(c) may not address collectibility challenges that are likely to be faced by certain other entities. Consider a typical licensing arrangement in the biotechnology industry in which the entity provides to a customer an initial license to intellectual property, performs research and development services for a fee for a limited period of time (e.g., 2 years), and is thereafter entitled to various payments based on customer achievement of development and commercialization milestones and royalties. It may be difficult for the entity to estimate collectibility of the amounts it could be entitled to over the entire duration of the contract, as the term of such contracts often exceeds 10 years. At the same time, the entity does not have any performance obligations beyond the 2 year term of the research and development services, and therefore would be unable to stop transferring goods and services in the contract in the event the customer fails to pay such milestones and royalties. This entity therefore will likely be unable to apply the provisions of paragraphs 606-10-55-3B and 3C to limit the extent of its consideration of collectibility, and may end up recognizing no revenue until completion of research and development services, when the provisions of paragraph 606-10-25-7(c) could be used. We do not believe such outcome is consistent with the FASB vision and the stated principles of ASC 606. A similar outcome could arise for any contracts that provide for a combination of (i) supply of multiple units of product (or delivery of services) over a period of time coupled with (ii) installment payments for such products or services. If collectibility of all installment payments cannot be assessed as of the future point when the entity is no longer supplying goods or services, revenue recognition would likely be precluded until completion of supply.

A further question arises when an entity, as a matter of practice, may operate a grace period policy under which it will stop providing goods or services to the customer when a customer fails to pay consideration when it becomes several months past due. Many companies in practice pay their vendors with a delay ranging from a few days to multiple months. Vendors in turn often adopt practical grace period policies under which recurring services will be suspended, or credit limits will be placed on hold, if the customer has not paid for more than a certain number of months of service, or if the amounts become a certain number of days past due. It is not clear to us whether such entities will be able to benefit from the provisions of paragraphs 606-10-55-3B and 3C, as in these instances the entity does not expect to stop supplies of goods or services when the customer does not pay consideration when it is due; instead, the entity will only stop supplies when the customer does not pay consideration when it is a certain number of days or months past due. Please note that we consider this example different from Example 1 Case C in the proposed revisions to ASC 606, where the entity does not have ability to assess collectibility as probable at the outset of an arrangement. In our mind, provided collectibility can be assessed as probable for a period at least equal to the grace period, it should be appropriate to recognize revenue in these circumstances. This is because the entity and the customer do have a valid contract in place and the consideration for the quantities of the product the entity is willing to supply to the customer is deemed collectible; the uncertainty is whether the



Exposure Draft: Proposed Accounting Standards Update, Revenue from Contracts with Customers (Topic 606), Narrow-Scope Improvements and Practical Expedients  
November 22, 2015  
Page 3

vendor is willing to provide for free several months of service to a customer who has stopped making payments, which we believe is akin to a volume (scope) concession.

The concept of volume (scope) concessions for some reason has not been explicitly addressed at all in ASC 606. Note that all references to concessions in the text of ASC 606 are to price concessions only. However, volume (scope) concessions also do happen, and on a regular basis in certain industries, whereby entities allow customers to receive a concession in the form of free product (e.g., additional units supplied for free) or free services (e.g., enhanced scope of professional services). A typical example is “make-good” free advertising impressions that online advertising companies habitually provide to their customers in excess of the committed contractual volume to ensure customer satisfaction. As we think through the framework of ASC 606, we believe volume/scope concessions should be viewed as potential deliverables that, if they can be estimated at the inception of an arrangement, will require allocating consideration. Volume (scope) concessions also could, and do, occur where at inception of the arrangement there was no expectation of granting them, in which case, in our mind, the framework for assessing contract modifications should be used to evaluate them.

As noted above, we believe an entity’s intent to terminate service to a customer after allowing a grace period is akin to a volume (scope) concession and as such should not preclude recognition of revenue.

*When the Entire Consideration Cannot Be Assessed As Collectible*

We believe there are other areas in ASC 606 as related to assessment of collectibility that remain problematic, for example, partial payment scenarios when collectibility of the entire consideration cannot be assessed as probable. Say, the entity cannot assess collectibility of amounts receivable from a customer due to its poor financial condition. If the entity is willing to supply goods and services to the customer in return for partial consideration that is paid upfront, with the remaining amounts due over time, this is likely because the entity has assessed the risks of collectibility and ensured that the amount received upfront is sufficient to provide a minimum required level of economic return, for example, via recovery of the entity’s costs. As such, the entity is willing to take on an economic risk of a lower margin in the event the customer does not pay the balance of the consideration, vs. the risk of finding an additional customer that does not have collectibility concerns. We believe this situation is not necessarily indicative of the entity being willing to provide a price concession to the customer since the entity expects to enforce the collection of the amounts due in the future. As such, the entity would not be able to limit its collectibility assessment to just the amounts received upfront. Under ASC 606, this contract would not be deemed a valid or genuine transaction until all goods or services have been supplied, or until substantially all payments have been received. However, in many instances we believe such assessment would not be reasonable because businesses look at credit risks in the same manner as performance (delivery), product quality, or any other risks, and are willing to take them even if a threshold of collectibility is not met for the entire amount of consideration. We also find it odd that the Board dictates that such contracts do not have substance, when business people with sound judgment who sign the agreement with the customer do believe substance exists, and most lay people we can think of would agree with this assessment. We noted statements in paragraph BC19 that appear to explain the Board’s view that in such circumstances “the alternate recognition model is the logical extension of the conclusion that a valid and genuine contact does not exist



Exposure Draft: Proposed Accounting Standards Update, Revenue from Contracts with Customers (Topic 606), Narrow-Scope Improvements and Practical Expedients  
November 22, 2015  
Page 4

between the entity and the customer”. Paragraph BC19 continues to explain that when “there is not a substantive contract between the parties, there can be no assurance that the payments received from the customer are solely for past performance”.

However, we believe the Board’s rationale in paragraph BC19 is inconsistent with the fact that under ASC 606 companies often may not know whether consideration they have received is for past or future performance, and this does not create challenges for judging that the contract is substantive. We noted above the case of volume (scope) concessions. When such concessions could exist, they would also create an uncertainty regarding whether the consideration received by the entity is related to past or future performance. A provision for return of products or a provision for delivery of goods or services contingent on external conditions could create uncertainties about whether consideration received relates to past or future performance. As a matter of fact, such uncertainty may exist in any multiple-element arrangement where the volume of products sold or services delivered could vary as part of the variable consideration provisions. Similarly, a potential to introduce a modification into any arrangement creates an uncertainty as to whether consideration received is related to past or future performance. One could also argue that under ASC 606 underlying principles, the concept of whether the consideration collected relates to past or future performance is in most instances irrelevant; as consideration, whenever collected, is allocated to all performance obligations; how much of the specific collected amount relates to which specific performance obligation(s) may or may not be known and does not matter.

Based on our considerations above, while we do support the basic concept in ASC 606 that in the absence of ability to estimate collectibility a substantive contract has not been entered into, we do not believe the Board has drawn the line at an appropriate place to separate substantive contracts from non-substantive. In our belief, inability to estimate collectibility of substantially the entire amount of consideration is too high of a hurdle. Instead, we encourage the Boards to refine the threshold and allow for recognition of revenue based on partial collections. One way to address this challenge is to revise the criterion in paragraph 606-10-25-1(e) to allow contracts to be deemed substantive if the entity can estimate total consideration that is probable of being received in the arrangement as related to the goods and services the entity is willing to supply to the customer. Setting the threshold at the level of partial consideration that is probable of being received simply introduces uncertainties into how much consideration the entity is entitled to, and how many units of product (what scope of services) the contract includes. We are not certain as to why entities should be precluded from estimating an outcome of these uncertainties any more than they are already able and expected to estimate outcomes of these same and multiple other uncertainties associated with recognition of revenue when those are triggered by issues unrelated to collectibility. It certainly does not appear reasonable to us that any potential inaccuracies associated with recognizing revenue based on such estimates would outweigh the impact of gross misalignments of entities’ financial statements with their economic performance patterns that would without a question result from implementation of the Board’s approach and the resulting recognition of the entire revenues in such arrangements in periods long after the performance has occurred. We do not believe the investors would appreciate having to read in an entity’s “Management Discussion & Analysis”, for example, that its revenue has increased 20% as a result of delivery of the final \$50,000 item under a contract where the collectibility criterion had not been previously met, and the entity had deferred the previously collected



Exposure Draft: Proposed Accounting Standards Update, Revenue from Contracts with Customers (Topic 606), Narrow-Scope Improvements and Practical Expedients  
November 22, 2015  
Page 5

\$10,000,000. We also do not encourage creating circumstances where entities can choose to deliver the final item in a desired quarter to create a significant one-time impact on their results of operations.

To reiterate, we do not advocate getting rid of the collectibility requirement as a contract recognition criterion in paragraph 606-10-25-1(e). However, we believe this criterion should be relaxed and become possible of being met based on an estimate of partial consideration that is deemed collectible. Such estimate would be subject to change from time to time, as the entity's assessment of collectibility would change. Contracts where no or only non-substantive amounts of consideration are deemed probable of being collected would still be deemed as having no substance. Non-substantive amounts can be defined, for example, as amounts that are inconsistent with the entity's pricing objectives, reasonable risk management policies, and progress towards satisfaction of the entity's performance obligations.

We draw the Board's attention to the fact that the proposed changes to ASC 606 already effectively allow for the consideration to be only partially collectible, provided the entity expects to stop the supply of goods and services when the customer fails to pay on the due date. Thus, our proposal is to simply make an additional step by removing the requirement for the entity to stop the supply of products or services in order to be able to use the partial collectibility provision. We do not believe the contract becomes substantive only because the entity is willing to stop the supply of products or services, and we likewise do not anticipate that investors and other users of the financial statements will find this notion reasonable. Also as noted above, we do not believe the Board's rationale in paragraph BC19 about inability to determine whether collected consideration relates to past or future performance is reasonable in view of the multiple scenarios under ASC 606 where the exact same challenge would exist and entities would be allowed and required to make estimates to recognize revenue.

#### *Reassessing Collectibility*

We also believe that the implementation of the proposed changes to ASC 606 should require entities to reassess collectibility on an ongoing basis beyond what is currently stated in paragraph 606-10-25-5 for those long-term contracts where the entity relied on the provisions of paragraph 606-10-55-3C and only assessed collectibility as probable during an initial time period. Effectively, this means that at inception the entity deemed collectibility to be probable during an initial period under the contract, and was unable to conclude collectibility was probable over a longer-term beyond this initial period. However, eventually the entity will enter into the period for which it did not initially have an ability to estimate collectibility as probable. Paragraph 606-10-25-5 does not allow the entity to reassess collectibility unless there is an indication of a significant change in facts and circumstances. Logically, this should lead the entity to conclude it should stop recognizing revenue when it enters into such period unless it can re-validate that the amounts receivable from the customer in what has now become the near-term future can now be assessed as probable of collection. In this regard, we do not believe the analysis in the Example 1 Case B, paragraph 606-10-55-98G, is consistent with the collectibility assessment reached at the inception of the arrangement. We also believe it is conceptually important in circumstances such as those described to reassess collectibility from time to time; this is because the customer's financial condition could have changed, and the fact that payments are ongoing may not be indicative of the customer's longer-term financial health in circumstances when the entity had initially concluded that the customer's financial



Exposure Draft: Proposed Accounting Standards Update, Revenue from Contracts with Customers (Topic 606), Narrow-Scope Improvements and Practical Expedients  
November 22, 2015  
Page 6

health over a long time period could not be estimated. We believe paragraph 606-10-25-5 and Example 1 Case B should be updated to align with these considerations.

### *Collectibility Roundup*

To close our thoughts, we want to emphasize that as much as we believe accounting principles and concepts should drive accounting answers, in setting such principles and concepts careful consideration

should also be given to how the investors and other users of the financial statements would perceive the outcome of their practical application. In this regard, we note that in the current practice there are multiple accounting areas that are complex to the point of being very poorly understood by anyone except a narrow group of expert technical accountants. Frequently, we hear that the finance and investor professionals disregard consideration of impact of any line items in the financial statements where such items reside (other income/expense is a typical one). Likewise, it is regrettable that some of the present revenue recognition rules, such as VSOE requirements of ASC 985-605, tend to render revenue amount non-indicative of the entity's performance, and changes in the deferred revenue line more important for investors than the actual revenues reported in the financial statements, while other companies are reported to make changes to their business or pricing in order to intentionally lose VSOE so that they can recognize their revenues over time akin to a cloud-services-like predictable annuity instead of hard-to-forecast upfront licenses. Considering the utmost importance of revenue reporting for most companies, we encourage the Board to continue to pursue the objective of facilitating the entities' ability to recognize revenues in a manner that would be aligned to their economic performance. We overall applaud the work undertaken by the FASB and the IASB in developing the revenue recognition standard; however, we observe that collectibility consideration is one of the few areas in the standard that, in our opinion, is not currently where it needs to be; it reads as if it was designed with punitive considerations in mind that dominated the accounting profession some 15-20 years ago. We do not believe it would be helpful to anyone if companies end up pointing at accounting rules for explanations of their financial performance, while investors and other users of the financial statements make embarrassing references to certain ASC 606 provisions.

### ***Responses to Board Questions***

The remainder of this document includes our responses to each of the "Questions for Respondents" posed in the Exposure Draft.

### **Comments on Questions for Respondents**

***Question 1:*** *Does the proposed addition of paragraphs 606-10-55-3A through 55-3C, as well as the addition of new examples, clarify the objective of the collectibility threshold? If not, why?*

**Response 1:** As we explained above, we believe that the proposed amendments improve the application of collectibility threshold in certain circumstances; however, they do not address collectibility challenges likely to be faced by other entities where we believe the relevant contracts should be deemed substantive and



Exposure Draft: Proposed Accounting Standards Update, Revenue from Contracts with Customers (Topic 606), Narrow-Scope Improvements and Practical Expedients  
November 22, 2015  
Page 7

revenue should be recognized in a manner consistent with the pattern of performance. Specifically, as noted above, we believe additional enhancements should be implemented via a further refinement of paragraph 606-10-25-1(e), to allow contracts to be deemed substantive when only partial consideration can be assessed to be probable of collection. This would require matching changes to paragraphs 606-10-55-3A through 3C.

We also want to draw the Board's attention to the proposed Example 1 Case A. In this example, arguments are made in paragraph 606-10-55-98 that the entity "has not satisfied its performance obligation to transfer control of the building to the customer", resulting in inability to apply the provisions of paragraph 606-10-25-7(c) to recognize revenue to the extent of the collected consideration, while paragraph 606-10-55-98A indicates that "the customer has not taken on the significant risks and rewards of ownership of the asset, because there is no contract between the parties in accordance with paragraph 606-10-25-1". As paragraph 606-10-25-7 is formulated, it is only meant to be applied whenever a contract with the customer does not meet the criteria in paragraph 606-10-25-1. If this situation in and of itself indicates, consistent with Example 1 Case A, that "the customer has not taken on the significant risks and rewards of ownership of the asset", it is not clear to us under what circumstances paragraph 606-10-25-7(c) could ever be applied. We believe, in Example 1 Case A, the key question is whether the entity is ready to give up ownership of the building for \$50,000. Although practically unlikely, if this were the case, in our mind, revenue, along with the associated loss, should be recognized, in accordance with paragraph 606-10-25-7(c), as there are no remaining performance obligations. However, in this example, based on the non-recourse nature of the receivable, one would argue that control to the building has not transferred based on the provisions of paragraph 606-10-55-68, as the entity effectively has the right to repurchase the building (contingent on the customer not paying for it). We believe this argumentation would be more in line with the intent of adding paragraph 606-10-25-7(c) to the standard. Alternatively, the amount of consideration paid for the building could be deemed non-substantive (refer to our proposal regarding definition of non-substantive consideration above).

**Question 2:** *Paragraph 606-10-25-7(c) was proposed to provide clarity about when revenue should be recognized for a contract that does not meet the criteria in paragraph 606-10-25-1. Does this proposed amendment improve the clarity of applying the guidance? If not, why?*

**Response 2:** As we explained above, we believe that the proposed amendments improve the framework for recognizing revenue in certain circumstances where previously a complete deferral would have been required and was not consistent with what we understand the Board's views are. However, as also described above, we believe the amendments do not address other circumstances where, in our mind, there are no good conceptual reasons to defer recognition of revenue. In this regard, we believe entities' ability to report financial performance should not be jeopardized by a concept that results in poor matching of accounting with performance and economic substance. When that is the case, we believe the concept should be modified to optimize the result. As we noted above, we believe the additional enhancements to paragraph 606-10-25-1(e) could address the challenges by allowing contracts to be deemed substantive when only partial consideration can be assessed to be probable of collection. This may obviate the need for some of the guidance in paragraph 606-10-25-7 which currently is effectively a reactive patchwork



Exposure Draft: Proposed Accounting Standards Update, Revenue from Contracts with Customers (Topic 606), Narrow-Scope Improvements and Practical Expedients  
November 22, 2015  
Page 8

addressing unintended outcomes from application of a principle that may not have been fully vetted. Additionally we want to highlight that paragraph 606-10-25-7 requires the entities to identify performance obligations and assess transfer of control and potentially determine and allocate transaction price as well as consideration received to performance obligations prior to concluding that the entity has a valid contract with a customer in scope of ASC 606.

**Question 3:** *The collectibility criterion in paragraph 606-10-25-1(e) refers to collectibility being probable, which is defined in Topic 606 as “likely to occur.” If the Board were, instead, to refer to collectibility being*

*“more likely than not,” which would result in a converged collectibility criterion with IFRS, would the amendment improve the collectibility guidance in Topic 606? Explain your response.*

**Response 3:** We do not believe it is desirable to reset the threshold for collectibility to “more-likely-than-not”. When contemplating our response to this question, we considered that paragraph 606-10-32-11 states that “an entity shall include in the transaction price some or all of an amount of variable consideration estimated in accordance with paragraph 606-10-32-8 only to the extent that it is probable that a significant reversal in the amount of cumulative revenue recognized will not occur”. To paraphrase, revenue recognition is deemed appropriate when the amounts of variable consideration are probable of being retained. We believe it would be inconsistent with the underlying principles of revenue recognition to set the threshold for collectibility at a lower level. This could also lead to what we would consider undesirable outcomes. For example, assume for a hypothetical contract with customer A, there is a 60% likelihood of collecting the arrangement consideration (which is all variable), and a 90% likelihood of retaining the entire amount of variable consideration. If the collectibility threshold were reset to the “more-likely-than-not” level, since the consideration is more likely than not to be collected, and is probable of being retained, the entire revenue would be recognized, even though there is only a slightly more than 50% (i.e., 54%, equal to 60% x 90%) combined likelihood of the entity receiving and retaining any amount of proceeds. Contrast this to a hypothetical contract with customer B where there is a 90% likelihood of collecting the arrangement consideration (which is also all variable) and a 60% likelihood of retaining the entire amount of variable consideration. The consideration is also more likely than not to be collected; however, none of it can be recognized in revenue as none of it is probable of being retained. As a result, revenue recognition for contract B is opposite of that for contract A. However, both contracts have the exact same combined likelihood (54%) of the entity receiving and retaining any proceeds. We do not believe the revenue recognition framework should allow for completely opposite results for what are to the entity two contracts with the same expected economic benefits at inception. We would also find it illogical to completely preclude recognition of revenue for contracts where, for example, consideration is partially collected upfront, with the collection of the remainder not deemed probable, while allowing companies to recognize in full revenue where no consideration has been collected, and the chances of collecting any amount of consideration could be barely over 50%.



Exposure Draft: Proposed Accounting Standards Update, Revenue from Contracts with Customers (Topic 606), Narrow-Scope Improvements and Practical Expedients  
November 22, 2015  
Page 9

**Question 4:** *Paragraph 606-10-32-2A provides a policy election that would permit an entity to elect to exclude all sales (and other similar) taxes collected from customers from the transaction price. Does this proposed amendment reduce the cost and complexity of applying Topic 606? If not, why?*

**Response 4:** We support the addition of paragraph 606-10-32-2A to provide to entities the ability to make a policy election to exclude all sales and similar taxes from customers from the transaction price. We believe this will reduce the complexity of complying with ASC 606 and also be aligned with the current accounting principles. We note that as originally released, ASC 606 would require an entity to include sales and similar taxes in the transaction price if the entity is the primary obligor for such taxes. This would require the entity to evaluate whether it is the primary obligor for taxes collected from customers on a jurisdiction by jurisdiction basis, which, in our opinion, would be overly complex while not providing much useful information to the users of the financial statements.

**Question 5:** *Revisions to paragraph 606-10-32-21 and the related example specify that noncash consideration should be measured at contract inception. Does this proposed amendment improve the clarity of applying the guidance? If not, why?*

**Response 5:** Overall, we agree with the Board's direction that noncash consideration should be measured at the inception of a contract. We do want to observe, however, that there appear to be other circumstances where consideration is likely to be measured at a different date, which is inconsistent with the Board's direction, and that further, the Board's guidance is likely to result in other accounting challenges.

First, we refer to transactions denominated in foreign currencies. While this is cash consideration, the associated challenges are somewhat similar to the challenges associated with measurement of noncash consideration, and the existing literature in Topic 830 is inconsistent with the Board's proposed guidance in paragraph 606-10-32-21. We note that ASC 606 does not presently contain any guidance regarding recognition of revenue for transactions where consideration is denominated in a foreign currency. Paragraph 830-20-30-1, however, stipulates that revenue should be recognized by measuring it into the entity's functional currency using the exchange rate in effect at the date the foreign currency transaction is recognized. This provision creates challenges regarding measurement of transaction price, its allocation to various performance obligations, handling of variable consideration, and other aspects of revenue recognition. As noted, it is also inconsistent with the Board's concept in the proposed revised paragraph 606-10-32-21, as well as the Board's clarifications in paragraph BC33 ("measurement date of the transaction price should not vary on the basis of the nature of the promised consideration"). We believe guidance in paragraph 830-20-30-1 and paragraph 606-10-32-21 should be aligned.

Further, if consideration, whether in noncash form or denominated in foreign currency, is measured at the inception of the arrangement, the question arises as to how to account for changes in the value of such consideration between the inception of the arrangement and the date the performance occurs and the related receivable or contract asset should be recognized. Certain forms of noncash consideration (such as financial instruments) must be carried at fair value, which would result in "Day 1" gain or loss recognition



Exposure Draft: Proposed Accounting Standards Update, Revenue from Contracts with Customers (Topic 606), Narrow-Scope Improvements and Practical Expedients  
November 22, 2015  
Page 10

on the performance date for the amount of the difference between the fair value initially measured at inception of the contract and that resulting on the performance date. We note that similar Day 1 gains or losses would result from the initial recognition of receivables from customers denominated in foreign currencies if that guidance is aligned with paragraph 606-10-32-21. In this regard, we believe it would be helpful to add clarifications to Topic 820, and in particular, include an example in paragraph 820-10-30-3A which lists frequent circumstances where the fair value of an asset acquired may differ from the transaction price upon initial recognition. We also presume based on the Board's reference to GAAP related to the form of the noncash consideration in Example 31, paragraph 606-10-55-250, that such Day 1 gains or losses would typically be included in other income or expense, as opposed to adjustments to revenue. To the extent that significant losses (or gains) may exist as of a balance sheet date with respect to executory customer contracts, it may be important for entities to disclose such amounts in the financial statements. Absent such disclosures, the disclosure of the entity's performance obligation amounts in accordance with paragraph 606-10-50-13 could be misleading for users of the financial statements if, for example, the amounts of future revenue that are disclosed based on inception-date measurement are also expected to result in a significant Day 1 loss for the entity from subsequent changes in the fair value of noncash consideration. Currently, ASC 606 does not require such disclosures.

Also, nonmonetary assets acquired as noncash consideration should be recorded at fair value in accordance with paragraph 845-10-30-1, which does not specify whether such fair value would be determined as of the inception of the arrangement or as of the date control is obtained (transaction date); we believe the existing practice tends to use the transaction date. Considering the absence of more specific guidance, it is not clear to us whether the Board intends to clarify how the existing guidance in paragraph 845-10-30-1 should be applied, whether the Board intends for entities to measure other assets received using fair value as of contract inception, not transaction, date, and whether and how entities would be required to account for the difference between the inception-date and the transaction-date fair values of the nonmonetary and other assets when such assets are not otherwise required to be carried at fair value. We believe clarification to paragraph 845-10-30-1 and possibly changes to other guidance would be appropriate if a change in practice is desired.

We also observe that aspects of recognition of revenue could have broad implications for areas unrelated to revenue. For example, the Board defined a new concept of control in paragraph 606-10-25-30. While vendors would be required to use this concept for purposes of recognizing revenue when transfer of control occurs at a point in time, we believe it would be reasonable for customers to consider whether they should use the same concept to determine when they should recognize assets (or expenses) they purchase from the vendors. Similarly, we are wondering if the Board's direction on measurement of transaction consideration at inception of the arrangement should be taken into account by customers in their determination of the amounts at which they should measure various assets (or expenses) they acquire. While the amounts recorded by customers and vendors with respect to the same transactions do not, conceptually speaking, have to mirror each other, mirroring would appear to be logical. We also note that paragraph 830-20-30-1 governs measurement of amounts denominated in foreign currencies not just for revenues, but also for expenses, gains, losses as well as assets and liabilities. In this regard, we are wondering if broader changes, or clarifications, to the application of this paragraph would be appropriate in view of the Board's direction with respect to paragraph 606-10-32-21.



Exposure Draft: Proposed Accounting Standards Update, Revenue from Contracts with Customers (Topic 606), Narrow-Scope Improvements and Practical Expedients  
November 22, 2015  
Page 11

**Question 6:** *Revisions to paragraph 606-10-32-23 clarify that the guidance on variable consideration applies only to variability in noncash consideration resulting from reasons other than the form of the consideration. Would the proposed amendments improve the clarity of applying the guidance? If not, why?*

**Response 6:** We believe that the proposed amendments improve the applicability of variable consideration guidance for noncash consideration, but are not necessarily the only reasonable method of addressing the issue at hand. In this regard, we do note that there could be circumstances whereby the value of the noncash consideration, for example, customer shares, would be directly affected by the entity's successful performance. Expectations of increases in customer share value that would be driven by vendor performance could also be built into the determination of the amount of noncash consideration (such as the number of shares) as a form of incentive to the vendor to perform. The Board's proposed guidance would require the vendor to disregard such factors when determining the amount of revenue it will be able to recognize; as we presume the vendor will reflect the increase in the value of the shares as other income, rather than revenue. We believe such outcome would be somewhat inconsistent with the fact that there could be a direct link between the entity's performance and the value of the noncash consideration it ultimately receives, i.e. the amounts recognized in other income could in reality be a direct result of the entity's ongoing major central operations.

**Question 7:** *Paragraph 606-10-65-1(f)(4) provides a practical expedient for contract modifications at transition. Would the proposed amendment reduce the cost and complexity of applying Topic 606? If not, why?*

**Response 7:** We support the addition of the new practical expedient in paragraph 606-10-65-1(f)(4) as in our mind it would significantly simplify transition for entities that may have entered into multiple modifications of their older contracts with customers. We do not believe there would be any practical effect on the quality of the financial information reported by such entities either at transition to ASC 606 or thereafter.

**Question 8:** *Revisions to paragraph 606-10-65-1(c)(2) clarify that a completed contract is a contract for which all (or substantially all) of the revenue was recognized under revenue guidance in effect before the date of initial application. Does this proposed amendment clarify the transition guidance? If not, why and what alternative would you suggest?*

**Response 8:** We support the revisions to paragraph 606-10-65-1(c)(2). In addition to resolving the stakeholders' concern regarding the use of the transfer of control notion as mentioned in paragraph BC44, we believe that this change will also significantly improve the quality of financial information reported by certain entities following the adoption of ASC 606. This will be the case for entities that have contracts where the entity will have completed its delivery obligations prior to adoption of ASC 606 but will not have yet fully recognized the contract revenue, usually due to such revenue not being deemed either fixed or determinable, or collectible. Many entities have multi-year contracts that could extend 10 years or longer; without this proposed revision, such entities could have had to continue to account for such contracts



Exposure Draft: Proposed Accounting Standards Update, Revenue from Contracts with Customers (Topic 606), Narrow-Scope Improvements and Practical Expedients  
November 22, 2015  
Page 12

under the ASC 605 guidance for extended periods of time. This would have resulted in significant lack of comparability between amounts of revenue reported by these entities for their own ASC 605 and ASC 606 contracts, and would have perpetuated the need for these entities to apply two different sets of complex revenue recognition rules at the same time. We sometimes observe similar circumstances in today's environment, when some entities still have to account for certain multi-year customer contracts based on the provisions of the long-superseded EITF 00-21, where such contracts have not been significantly modified after the entities' adoption of EITF 08-3. This results in challenges to both entities and users of the financial statements, as similar contracts have different accounting treatment that affects the reported results of the entities' performance. We are happy to see the revisions to ASC 606 that will minimize the extent of reporting required to be done by the same company using two different sets of rules for similar contracts. We do want to highlight that the proposed revisions will likely result in significant amounts of "recycling" (re-recognition) of revenue previously recognized under ASC 605 in circumstances where an entity previously considered the amounts not collectible and followed cash basis of recognition, and under

ASC 606 as currently formulated would include such amounts in deferred revenue as of the adoption date and recognize revenue when one of the triggering events in paragraph 606-10-25-7 occurs.

Also as a matter of a proposed technical correction, we believe it would be helpful to add to the standard that entities adopting ASC 606 retrospectively in accordance with paragraph 606-10-65-1(d)(1) will also need to follow some of the guidance in paragraph 606-10-65-1(h), specifically, to recognize the cumulative effect of initially applying ASC 606 as an adjustment to the opening balance of retained earnings of the annual reporting period that includes the earliest date presented in the financial statements. In this regard, we find how the modified retrospective adoption method has been described in paragraph 606-10-65-1(d)(2) to be confusing, because the cumulative effect of initially applying ASC 606 would need to be recognized by all entities, regardless of the adoption method they select.

Last, we would like to reiterate our recommendation from our comment letter dated May 28, 2015 regarding the deferral of the effective date of ASC 606. We observe that the standard has not yet been finalized as of late 2015, and we understand it is not expected to be finalized until sometime into 2016. The TRG continues its deliberations, and additional recommendations of changes to the standard are likely to arise. As far as we know, most software developers do not yet have sophisticated products that entities could use to help implement the new standard. As a result, there is going to be less than two full years, perhaps as little as 18 months, remaining for companies to adopt ASC 606 at the time the standard will become final. We also observe that with the ongoing FASB deliberations, many companies have lost the initial momentum to initiate the implementation actions. Apart from really large entities, most implementation efforts have not started or have started and stalled. Considering the ongoing redeliberations and their developing perception in the industry, we do not believe this situation can change until the standard becomes truly final. We do encourage the Board to re-address the issue of the standard's effective date, as we believe it is time to contemplate an additional one-year deferral, and to also determine and stick to a plan to end the deliberations and finalize the standard.



Exposure Draft: Proposed Accounting Standards Update, Revenue from Contracts with Customers (Topic 606), Narrow-Scope Improvements and Practical Expedients  
November 22, 2015  
Page 13

We would be pleased to respond to any questions the FASB or its staff may have concerning our comments. Please direct any questions to partners in our Accounting Standards and Professional Practice group:

- Aleks Zabreyko (650-353-7044, [aleks.zabreyko@connorgp.com](mailto:aleks.zabreyko@connorgp.com)) or
- Denis Kozhevnikov (650-521-3099, [denis.kozhevnikov@connorgp.com](mailto:denis.kozhevnikov@connorgp.com)).

Sincerely,

*Connor Group, Inc.*