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April 17, 2019

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

RE: Proposed Accounting Standards Update, *Codification Improvements—Share-Based Consideration Payable to a Customer* (File Reference No. 2019-400)

Dear Technical Director:

We appreciate the opportunity to comment on the proposed ASU, *Codification Improvements—Share-Based Consideration Payable to a Customer*.

We appreciate the Board's efforts to provide guidance on how companies should measure share-based payments to customers and the complexity involved in a measurement date approach under either Topic 718 or Topic 606. We believe that in order to make the selected approach operational and reduce diversity in how the proposal is applied, additional guidance is needed to clarify some of the proposals and their interaction with Topic 606. Specifically, we believe the Board should consider providing guidance related to:

- Revenue recognition before the grant date;
- When a customer is no longer a customer; and
- Award and contract modifications.

We recommend that the Board clarify that the accounting for certain awards may require an entity to estimate the value of share-based payments to customers **before** a grant date for the award has been established. That accounting may apply in circumstances in which an entity promises or intends to provide a share-based award to a customer at or after inception of a revenue contract or when accounting for certain award modifications. This would be similar to the guidance in Topic 718 for circumstances in which the service inception date precedes the grant date. Our response to Question 3 provides further details.

We also recommend that the Board modify the language in paragraphs 718-10-35-10(e) and 718-10-35-11 to clarify that an award to an employee is subject to guidance other than Topic 718 only if the award is modified after it has **vested** and the grantee is no longer an employee. The proposals might be read to say that the award is subject to other guidance when an employee becomes a nonemployee, even if the award is not yet vested and the award is not modified.

Our responses to the Board's specific questions are included in the Appendix to this letter.

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If you have questions about our comments or wish to discuss the matters addressed in this comment letter, please contact Kimber Bascom at (212) 909-5664 or kbascom@kpmg.com, Regina Croucher at (212) 954-1285 or rcroucher@kpmg.com, or Meredith Canady at (212) 909-5858 or mcanady@kpmg.com.

Sincerely,

KPMG LLP

KPMG LLP

Appendix – Responses to Questions for Respondents

Question 1 – Measurement date

Do you agree that share-based payment awards issued to customers as consideration payable should be measured at the grant date of the award? If not, why should there be a difference between the measurement date for share-based payment awards issued to customers and nonemployee share-based payment awards, and what other alternatives would be more appropriate?

We appreciate the Board's decision to require an entity to measure share-based payment awards issued to a customer as consideration payable at the grant date to achieve consistency in reporting. We understand the complexity involved as both measurement date approaches under Topic 718 or 606 add complexity to the subsequent accounting under those Topics.

We recognize that using the grant date of the share-based payment award as the measurement date may not always result in an economic value of the award on the grant date that represents the economic value of the contract entered into by an entity and its customer. In the master supply agreement example in BC13 and BC14, we believe that a customer makes a business decision to order a good or service from an entity based on the economics on the date on which it places a purchase order, not on the date on which it enters into the master supply agreement. Consider the accounting outcome under the proposals if the master supply agreement in the example in BC13 was evergreen but pricing of the goods or services was renegotiated periodically without an award modification. Under the proposals, the same grant date fair value established at inception of the master supply arrangement could then be used in perpetuity, even though the renegotiated pricing of the goods or services and the customer's subsequent purchasing decisions considers the change in economic value of those awards. Consequently, we believe that measuring the share-based payment award using the contract inception date under Topic 606, which would be the purchase order dates under the master supply agreement example in paragraphs BC13 and BC14, may better reflect the economic value of the award to the entity and to the customer.

While we believe that the proposals may depart from a core principle of Topic 606, we acknowledge the Board's efforts to identify an approach that is more straightforward than the accounting under that Topic, thereby making it potentially less complex for preparers to implement. We agree with the Board that measuring the awards under Topic 718 would typically be less complex and would provide consistency with the model for measuring other nonemployee awards. Furthermore, we believe that the Board's proposals may reduce diversity in practice in situations in which the grant date occurs before the contract inception date under Topic 606. However, diversity in practice may arise or continue to exist when an entity promises or intends to provide a share-based award to a customer before a grant date for the award has been established or when accounting for contract and award modifications. Refer to our response to Question 3 for further observations and proposed clarifications.

Question 2 – Classification requirements

Do you agree that share-based payment awards issued to customers as consideration payable should be classified in accordance with the guidance in Topic 718?

Yes. We believe that share-based payment awards issued to customers as consideration payable should be classified under Topic 718.

Question 3 – Sufficiency of guidance

Do you agree that the amendments in this proposed Update provide sufficient guidance to account for share-based consideration to a customer?

No. Assuming the Board issues a final ASU that is based substantially on the proposals, we believe some additional clarifications are necessary.

Revenue recognition before grant date

We believe further guidance is needed in circumstances in which revenue is recognized before a grant date is established. The example in BC13 and BC14 addresses a fact pattern in which a grant date occurs before a contract exists under Topic 606. In those circumstances, additional guidance is not necessary. However, it is likely that the guidance in the proposed ASU and Topic 606 may be applied inconsistently if a contract exists under Topic 606, and an entity promises or intends to provide a share-based award to a customer before a grant date for the award has been established.

Paragraph 606-10-32-27 states that an entity recognizes a reduction of revenue from consideration payable to a customer at the later of the date on which the entity recognizes revenue or the entity ‘promises to pay’ the customer (referred to as the ‘later of’ guidance). An entity may promise to pay a customer before it meets the grant date requirements. In November 2015, the FASB’s Revenue Transition Resource Group (TRG) discussed when an entity should apply the later of guidance instead of the variable consideration guidance (TRG Paper 37). The TRG consensus at the 2015 meeting was that an entity does not apply the later of guidance when either the entity intends to provide consideration to the customer when the parties enter into the contract, or the customer has a reasonable expectation that the entity will provide consideration to it based on customary business practices. In either of those circumstances, the entity would account for the variable consideration under paragraph 606-10-32-14, which may require the entity to estimate the value of an expected award before a grant date is established.

It is unclear how an entity that has a past practice of providing share-based payment awards to customers or that otherwise promises or intends to provide an award would account for that practice or intent before the grant date under Topic 718 has occurred. Even if a reasonable expectation of an award does not exist at inception of a contract under Topic 606, it is unclear whether and, if so, by what amount, the entity would reduce revenue when it promises an award to a customer after revenue is recognized but before a grant date for an award has been established.

Some preparers may conclude that because the proposed ASU would establish the measurement date as the grant date, the entity cannot recognize a reduction in revenue before the grant date. We believe that view may inappropriately overstate revenue by delaying the recognition of expected revenue reductions, therefore violating a core principle of Topic 606 (i.e. to recognize revenue equal to the consideration to which an entity expects to be entitled).

We recommend that the Board clarify the proposals to state that an estimate of the value of share-based payments to customers may be required in circumstances in which the entity promises or intends to provide a share-based award to a customer before a grant date for the award has been established. In these cases, the entity would subsequently adjust the estimated value attributable to the form of the consideration before the grant date to reflect the measurement on the grant date as required by the proposed ASU. We believe this outcome would be similar in concept to how an entity accounts for awards when the service inception date precedes the grant date and, therefore, doing so would be consistent with the measurement principles of Topic 718.

Grantee is no longer a customer

Paragraphs 718-10-35-10 and 11 indicate that share-based payment awards to customers are no longer within the scope of Topic 718 when a grantee vests in the award and is no longer a customer. We recommend that the Board clarify when the grantee would no longer be a customer. Topic 606 defines a customer as “a party that *has* contracted with an entity to obtain goods or services....” Diversity in practice could arise based on whether an entity takes a contract-specific view or a broad view of when the grantee is no longer a customer.

Once an entity fulfills its obligations under the contract (e.g. the purchase order in the BC13 and BC14 example) and consideration is paid to an entity, a revenue contract no longer exists. An entity could view the contract-specific fulfillment as the date at which the grantee would no longer be a customer. Under this view, a modification of the award after the fulfillment date (assuming the award was fully vested on the fulfillment date) would not be in the scope of Topic 718. Alternatively, an entity could take a broad view of when the grantee is no longer a customer and continue to account for a modification of an award within the scope of Topic 718 because the grantee either continues to order or is expected to order goods or services from the entity in the future under separate contracts (e.g. purchase orders in the BC13 and BC14 example).

We believe a broad view of the term customer is appropriate and consistent with how preparers evaluate whether an entity is a customer, to determine whether a payment to a customer is for a distinct good or service. This is also consistent with how preparers determine if a customer relationship intangible asset exists in a business combination. The ambiguity of when a grantee is no longer a customer may also affect how a nonpublic entity applies the practical expedient in paragraphs 718-10-30-20A and 20B. Clarifying the Board’s intent would help to ensure the guidance is consistently applied.

Award and contract modifications

In addition to our observations about how to account for award modifications when a grantee is no longer a customer, we believe further clarification is needed about the interaction between the guidance for award modifications under Topic 718 and contract modifications under Topic 606. The proposals would require the entity to measure the award on the grant date under Topic 718. Paragraph 606-10-32-25A of the proposed ASU states, “any changes due to the form of the consideration shall be reflected elsewhere in the grantor’s income statement.” This could be interpreted to mean that modifications of customer awards do not affect the amount of revenue

recognized. We believe a modification to a customer award is a change in transaction price that should be accounted for as a contract modification under Topic 606. However, it is not clear that the proposals would produce that outcome, thus, we are concerned about the potential for diversity in application of the guidance to award modifications.

Even if an entity determines that award modifications are revenue contract modifications, situations could arise in which the timing of the award modification under Topic 718 differs from the contract modification under Topic 606. For example, parties can agree to a change in scope of a revenue contract even if a change in price has not been approved. In these cases, the contract modification guidance in Topic 606 is applied and the modified transaction price that is yet to be determined is deemed to be variable consideration. Similar to our observations related to revenue recognition before the grant date, we believe there could be confusion about when to account for variable consideration as a result of an award modification, because the measurement of the award in the proposed ASU is based on the Topic 718 grant date. We recommend that the Board clarify that the accounting for certain award modifications may require an entity to estimate the value of share-based payments to customers if a contract modification occurs before an award modification date.

We believe that further clarification is needed about when an entity would need to determine a new grant date for measuring awards. In the example in BC13 and BC14, an entity would determine the grant date fair value of an award on the date that a master supply agreement (MSA) is agreed to by both parties. In practice, there are a broad range of arrangements that would be in the scope of this guidance. In some of those arrangements, it would be unclear what would trigger an entity to determine a new grant date fair value for awards granted to that same customer. For example, consider an MSA which provides for the grant of a specified number of shares for a specified volume of sales of its products, with no limit on the cumulative number of shares that could be earned. Also assume that the MSA automatically renews each period or the MSA is extended, but the entity does not change any of the terms of the arrangement. The proposal is unclear if the renewal or extension would constitute a new grant date and, if so, how that would be distinguished from the grant date for transactions that occurred during the original period of the MSA. In addition, we note that the renewal would not be considered to be a contract modification under Topic 606. In other cases, an entity and customer may operate under an evergreen MSA in perpetuity, but pricing is renegotiated on a regular basis. We believe that under Topic 718 it is not clear that there would be a new grant date in these scenarios because the underlying awards have not been modified despite the fact that renegotiated prices of the goods or services and the customer's subsequent purchasing decisions are based on an economic value of the awards that may not be different from the grant date value. The Board's intent in these scenarios is unclear and the proposals may not be interpreted and applied consistently. We recommend that the Board clarify when changes to contract terms would require an entity to determine a new grant date when measuring awards.

Question 4 – Proposed transition requirements

Are the transition requirements for the proposed amendments appropriate? If not, what transition approach would be more appropriate and why?

Yes. We believe the transition requirements for the proposed amendments, which would align the transition and effective date requirements with those of ASU 2018-07, are appropriate.

Question 5 – Effective date

How much time would be necessary to adopt the proposed amendments? Should early adoption be allowed?

We believe that the proposed amendments should be effective for all entities for fiscal years beginning after December 15, 2019.

We believe that early adoption of the proposed amendments should be permitted for periods for which the financial statements have not been issued, but no earlier than an entity's adoption date of ASU 2018-17.