

American Institute of CPAs 220 Leigh Farm Road Durham, NC 27707-8110

March 15, 2012

Susan M. Cosper, CPA Technical Director FASB 401 Merritt 7 PO Box 5116 Norwalk, CT 06856-5116

Re: November 14, 2011 Exposure Draft of a Proposed Accounting Standards Update (ASU)--Revised, *Revenue Recognition (Topic 605): Revenue from Contracts with Customers* [File Reference No. 2011-230]

Dear Ms. Cosper:

One of the objectives that the Council of the American Institute of Certified Public Accountants (AICPA) established for the PCPS Executive Committee is to represent the views of local and regional firms on professional issues in keeping with the public interest, primarily through the Technical Issues Committee (TIC). This communication is in accordance with that objective. These comments, however, do not necessarily reflect the positions of the AICPA.

TIC has reviewed the Revised ED and is providing the following comments for your consideration.

GENERAL COMMENTS

TIC believes the Revised ED represents a significant improvement over the original ED. The specific comments below address remaining issues concerning clarity of the guidance and the need for additional illustrative examples.

SPECIFIC COMMENTS

Question 1: Paragraphs 35 and 36 specify when an entity transfers control of a good or service over time and, hence, when an entity satisfies a performance obligation and recognizes revenue over time. Do you agree with that proposal? If not, what alternative do you recommend for determining when a good or service is transferred over time and why?

Control

TIC agrees with the Boards' proposal to base the recognition of revenue on a transfer of control to the customer with the use of control-based concepts to determine the timing of revenue recognition and with the proposed definition of control. However, TIC believes the practical application of a control model differs for goods, services or rights to use the entity's assets.

Application of a control concept to the non-goods categories will be challenging. TIC requests more robust supporting guidance and welcomes the Boards' efforts to provide indicators of when control is transferred and specific examples of how to apply the necessary judgments and disclosure for each of the different categories (i.e., services, work-in-progress or the right to use an entity's assets). TIC believes that a control principle is operational only if supported with appropriate guidance/discussion of the concepts to be considered in its application. TIC believes the following example represents part of the necessary guidance that should be included in the final standard:

 A service contract—An entity has entered into a consulting contract to develop a strategic plan for another entity for a fixed fee. The service is provided over time, and control is given to the customer at various points as items are delivered. However, until the plan itself is delivered, the contract has not been fulfilled. This example could include various revenue recognition considerations that would be needed to properly analyze this type of service contract.

Practicability of alternate use

When evaluating whether an asset has an alternative use to the entity, an entity shall consider at contract inception the effects of contractual **and practical limitations** on the entity's ability to readily direct the promised asset to another customer (paragraph 36). TIC supports this concept but believes more examples are needed to illustrate the types of practical limitations that would cause the entity to conclude that it has not created an asset having an alternative use, as discussed in paragraphs 35(b) and BC94. Based on the examples given in the ED, some may believe that practical limitations relate to cost issues only; whereas others may have a different point of view as to the scope of the term. Without further guidance, inconsistencies in practice may occur. TIC recommends the following examples for inclusion in the final standard to illustrate the practical limitations that could arise in various types of contracts:

- Assets (such as a building) constructed on the customer's property. The entity could not take it back and sell it to another customer.
- Production of boxes stamped with the customer's logo. Once the logo is on the box, the box cannot be re-sold to another customer.

• Licensing customized R&D technology to customers. Describe various types of practical limitations that could arise for either the seller or the customer that would affect the seller's recognition of revenue.

Temporary control

TIC shares the concern expressed in the Alternative View (paragraph 375) regarding the accounting for revenue to be recognized for licensing arrangements, sales-based royalty payments for intellectual property and other instances of temporary control, such as sales with a lengthy right of return or momentary ownership of an asset. TIC recommends the Board clarify temporary v. non-temporary control and differentiate temporary control related to goods/products (leasing) and services (if any). In particular, additional guidance may be necessary to differentiate royalty licenses, consignment sales and goods sold with rights of return.

For example, TIC is aware of certain arrangements in the pharmaceutical industry that permit a right of return period of up to one year and other arrangements in the retailing industry that permit the customer (e.g., Walmart) to take advantage of an unlimited right of return with its suppliers. Examples should be added to the final standard to explain how the guidance on rights of return, put options and consignment sales would be applied to such situations.

Question 2: Paragraphs 68 and 69 state that an entity would apply Topic 310 (or IFRS 9, if applicable) to account for amounts of promised consideration that the entity assesses to be uncollectible because of a customer's credit risk. The corresponding amounts in profit or loss would be presented as a separate line item adjacent to the revenue line item. Do you agree with those proposals? If not, what alternative do you recommend to account for the effects of a customer's credit risk and why?

TIC agrees with the Boards that revenue should be recognized at the amount of consideration to which the entity expects to be entitled. TIC also supports the Boards' conclusion that a company would exclude expectations of collectibility when determining the transaction price and should therefore recognize revenue at the "gross" amount, with the effect of customer credit risk accounted for separately.

However, the ED would also require that the effects of the customer's credit risk be reflected as a separate line item adjacent to the revenue line item. TIC does not think that the Board should dictate where the effect of the credit risk should be presented on the statement of operations. While the reporting enterprise should provide transparent disclosure of the potential impairment loss as a result of the customer's credit risk, there is no direct connection between revenue recognized in particular reporting periods and impairment losses recognized in that reporting period. Indeed, there may be no direct connection between the reporting entity's economic and operational performance and the factors that impact the customers' credit risks.

The impact of the credit loss is not materially different from the other risks and losses that an entity may have experienced in operating a business. An entity should have the flexibility to decide what would be the most appropriate presentation and disclosures to reveal the losses to the users of its financial statements. For example, presenting the effect of credit risk as a contra-revenue item would be an appropriate conclusion for a manufacturer or retailer. However, health care institutions want to distinguish charity care and contractual allowances from patient bad debts and may prefer a split presentation approach whereby charity care and contractual allowances are presented as contra-revenue and credit losses from patients are presented within the expense section of the statement of operations.

TIC therefore recommends that flexibility be permitted in the placement of the effects of credit risk. TIC believes such flexibility will evolve along industry lines in a manner that will most accurately portray the substantive performance of an entity and will result in a presentation that is relevant for the respective financial statement users. It has the added advantage of being a principles-based approach that would result in minimal changes in current practice. Under TIC's proposed approach to provide presentation options, the entity should be required to disclose its accounting policy related to the effects of credit risk.

Question 3: Paragraph 81 states that if the amount of consideration to which an entity will be entitled is variable, the cumulative amount of revenue the entity recognizes to date should not exceed the amount to which the entity is reasonably assured to be entitled. An entity is reasonably assured to be entitled to the amount allocated to satisfied performance obligations only if the entity has experience with similar performance obligations and that experience is predictive of the amount of consideration to which the entity will be entitled. Paragraph 82 lists indicators of when an entity's experience may not be predictive of the amount of consideration to which the entity will be entitled in exchange for satisfying those performance obligations. Do you agree with the proposed constraint on the amount of revenue that an entity would recognize for satisfied performance obligations? If not, what alternative constraint do you recommend and why?

TIC supports the general principle of paragraph 81 but dislikes the term "reasonably assured." Use of this term will be confusing in comparison to ASC 310-10-35-10 (Losses from Uncollectible Receivables), which apparently is not being amended by the Codification Amendments ED issued on January 4, 2012. The requirements of ASC 310-10-35-10 are based on whether it is probable that the entity will be unable to collect all amounts due (the "probable" terminology).

TIC therefore agrees with the Alternative View presented in paragraph BC376(b) that the term should be removed or a better term used. TIC prefers the use of the "probable" terminology. It is well understood and, if retained, would minimize unnecessary change and eliminate a potentially new, undefined term from the literature. If the Boards decide the "reasonably assured" language should be retained, it should be a glossary term and should be distinguished from the notion of "probable." The definition should incorporate

the discussion in paragraphs BC201 (last sentence) and BC202-203. These paragraphs imply that the notion of reasonably assured is not meant to include collectibility factors.

Question 4: For a performance obligation that an entity satisfies over time and expects at contract inception to satisfy over a period of time greater than one year, paragraph 86 states that the entity should recognize a liability and a corresponding expense if the performance obligation is onerous. Do you agree with the proposed scope of the onerous test? If not, what alternative scope do you recommend and why?

TIC agrees with the proposed scope of the onerous test in the Revised ED.

Question 6: For the transfer of a nonfinancial asset that is not an output of an entity's ordinary activities (for example, property, plant, and equipment within the scope of Topic 360, IAS 16, or IAS 40), the Boards propose amending other standards to require that an entity apply (a) the proposed guidance on control to determine when to derecognize the asset and (b) the proposed measurement guidance to determine the amount of gain or loss to recognize upon derecognition of the asset. Do you agree that an entity should apply the proposed control and measurement guidance to account for the transfer of nonfinancial assets that are not an output of an entity's ordinary activities? If not, what alternative do you recommend and why?

TIC supports the proposed amendments to require an entity to apply the recognition and measurement principles of the Revised ED to nonfinancial assets (including property, plant and equipment within the scope of Topic 360 and intangible assets within the scope of Topic 350). TIC also agrees that the entity should not recognize revenue in these transactions but instead should recognize gains or losses, as appropriate, which would be classified as other income (expense).

Disclosures

Disaggregation of Revenue

TIC welcomed the Board's proposal (paragraph 116) that a nonpublic entity need not apply the disclosure requirements in paragraph 114 and 115 for the disaggregation of revenue.

Tabular Reconciliation of Contract Assets and Liabilities

TIC welcomed the Board's proposal that a nonpublic entity may elect not to provide a reconciliation of contract balances (paragraph 117), the amount of transaction price allocated to remaining performance obligations (paragraph 119), a reconciliation of liability balances recognized from onerous performance obligations (paragraph 123), and a reconciliation of asset balances recognized from the costs to obtain or fulfill a contract with a customer (paragraph 128). It is not cost-beneficial for a nonpublic entity to provide these disclosures as the stakeholders of the nonpublic entities most likely will have access to such information.

Transition

TIC members could not agree on a preferred transition method. Some support retrospective application, while others believe retrospective application will be burdensome for many entities. These members generally support the point of view expressed by the Private Company Financial Reporting Committee (PCFRC), which recommended that retrospective application should not be required for nonpublic entities. The PCFRC preferred an optional approach that would instead allow disclosure of the retroactive impact of the Proposed ASU.

TIC appreciates the opportunity to present these comments on behalf of PCPS member firms. We would be pleased to discuss our comments with you at your convenience.

Sincerely, Karen Kerber

Karen Kerber, Chair

PCPS Technical Issues Committee

cc: PCPS Executive and Technical Issues Committees