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March 13, 2012

Technical Director
File Reference No. 2011-230
Financial Accounting Standards Board
401 Merritt 7, PO Box 5116
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Sent via email to director@fasb.org,

Re: Proposed Accounting Standards Update (Revised)—*Revenue Recognition (Topic 605): Revenue from Contracts with Customers*, File Reference No. 2011-230 (“Revised Exposure Draft”)

Hewlett-Packard Company (“HP” or the “Company”) appreciates the opportunity to share our company’s view on the Revised Exposure Draft outlining the framework for revenue recognition from contracts with customers.

As indicated in our October 2010 response to the original exposure draft issued June 4, 2010, we firmly support the move towards a single global revenue recognition model, which will produce consistent and comparable financial statements reflecting the economic substance of underlying transactions and, therefore, be more meaningful to investors. However, while the Boards moved significantly in the direction to make the standards more practical to implement, as noted in our responses below, we feel that a number of the provisions will impose costs that do not provide sufficiently valuable benefits to users or analysts.

In the Revised Exposure Draft, the Boards asked a number of specific questions. We offer our comment on those questions as well as other key aspects of the Revised Exposure Draft.

Question 1: Recognition when transfer of control of a good or service is over time

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?

HP Response: HP is supportive of the proposed recognition methods for performance obligations satisfied over time.

Question 2: Presentation of credit risk as a separate line item adjacent to the revenue line item

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?

HP Response: Given that credit risk is no longer to be considered in determining the transaction price, HP does not support specifically presenting “bad debt expense” adjacent to the revenue line item. Because the unconditional right to consideration (i.e., a receivable) and a contract asset is to be accounted for under Topic 310, *Receivables*, we believe presentation of bad debt expense should be excluded from the scope of the revenue standard. If the current guidance is retained, HP does not believe that bad debt expense should be presented adjacent or within the revenue line item. Instead, we would propose classification of bad debt expense as an operating expense, consistent with current application, with a rollforward of the allowance for doubtful accounts presented in the footnotes to the financial statements.

Question 3: Cumulative amount of variable consideration limited to amounts reasonably assured, if entity’s experience is predictive of the amount of consideration to which the entity will be entitled.

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?

HP Response: HP agrees that revenue recognized under a contract for satisfied performance obligations should be limited to the amount to which the entity is reasonably assured to be entitled. In circumstances where variable consideration relates to unsatisfied performance obligations, HP requests greater clarification to the indicators in Paragraph 82 detailing when such estimates would be reasonably assured.

Additionally, for entities that frequently enter into arrangements to provide services on a long-term basis, and the potentially significant effect the determination of separate performance obligations can have on the allocation and recognition of variable consideration in these arrangements, HP asks for further clarity around how the Boards recommend an entity should make such a determination for long-term service arrangements.

As it relates to allocating variable consideration, the requirement to allocate consideration to a single performance obligation could significantly change the timing of revenue recognition from current practice. HP requests further guidance or illustrative examples in certain specific situations. For example:

- The proposed guidance suggests that the variable consideration, and subsequent changes in variable consideration, be allocated to a single performance obligation. It is not clear whether this exception can be applied if the variability in the total transaction price is attributable to more than one but not all of the performance obligations in the arrangement.
- It is not clear how an entity treats the fixed consideration in the arrangements where the variable consideration is allocated to a single performance obligation. That is, would the entity also allocate any of the fixed consideration to that performance obligation, or is the entity precluded from doing that because the entity determined the variable consideration relates to that particular performance obligation?
- For entities that have multiple payment streams that are all variable, is it possible to determine that some of the variable payment streams are related to only certain performance obligations, but the other variable payment streams are related to all of the goods and services in the arrangement?

HP would like to see greater clarity and detail in the criteria a company would utilize to determine whether the variable consideration should be estimated and items to consider when calculating the estimate.

Question 4: Onerous performance obligations recognized at the performance obligation level, when, at its inception, the obligation will be satisfied over a period greater than one year.

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?

HP Response: While we recognize the Boards' desire to account for changes in assets and liabilities at the performance obligation level (unit of account), and welcome the exclusion for obligations of less than one year, we strongly believe the application of the onerous test should be at the overall agreement level for all remaining obligations rather than individually for each distinct performance obligation within the agreement.

Paragraph 30 of the Revised Exposure Draft provides a practical expedient for combining distinct obligations as a single performance obligation in situations where there is the same pattern of transfer to the customer, such as two distinct services over the same period of time. Furthermore, entities can account for those services as one performance obligation if applying one method of measuring progress would faithfully depict the pattern of transfer. It is not clear if this expedient also applies to two or more services that have a delivery pattern that may differ over the same period (i.e., a service delivered evenly over the period and a service that may be delivered unevenly over that same period). Additionally, when determining if the measure of progress is similar, it is unclear how issuers should compare the measurement method to conclude if they meet the requirements of applying the practical expedient.

As an example, assume an entity enters into an IT outsourcing agreement to deliver multiple services over the same period of time. The delivery of the services are expected to fluctuate at different times within that same period based on expected changes to the customers needs and usages over time. However, in that same example, the progress of each service is measured based on output methods as described in paragraphs 41-43. These output methods may differ slightly between each service based on different output measures (number of calls to a helpdesk, number of users or units supported). In this example, all services are to be delivered over the same time period and the measure of progress is the same (output method). It is our view that services included in such arrangements with similar fact patterns should be viewed as a single performance obligation. We would encourage other examples of where this practical expedient can and cannot be applied considering assumptions similar to the one provided above.

Further, we believe the requirement to perform an onerous test at the performance obligation level is not necessarily representative of the broader, integrated economics of the arrangement, the company's go-to-market strategy for these types of arrangements, and the way we negotiate and price our arrangements with customers and, as such, the disclosure and reporting required for individual component margins through an onerous test at the performance obligation level would not provide decision useful information to investors.

We believe the onerous test should reflect the amount that the total expected costs for remaining performance obligations exceed the carrying amounts of those obligations. We, therefore, request the Boards to expand the definition of a 'distinct performance obligation' to allow for consideration of the overall pricing and profitability of a contract, given such attributes are fundamental to management and investors, in assessing the overall economics of an arrangement.

Question 5: Disclosure Requirements

Question 5: The Boards propose to amend Topic 270 and IAS 34 to specify the disclosures about revenue and contracts with customers that an entity should include in its interim financial statements. The disclosures that would be required (if material) are:

- 1. The disaggregation of revenue (paragraphs 114–116)**
- 2. A tabular reconciliation of the movements in the aggregate balance of contract assets and contract liabilities for the current reporting period (paragraph 117)**
- 3. An analysis of the entity’s remaining performance obligations (paragraphs 119–121)**
- 4. Information on onerous performance obligations and a tabular reconciliation of the movements in the corresponding onerous liability for the current reporting period (paragraphs 122 and 123)**
- 5. A tabular reconciliation of the movements of the assets recognized from the costs to obtain or fulfill a contract with a customer (paragraph 128).**

Do you agree that an entity should be required to provide each of those disclosures in its interim financial statements? In your response, please comment on whether those proposed disclosures achieve an appropriate balance between the benefits to users of having that information and the costs to entities to prepare and audit that information. If you think that the proposed disclosures do not appropriately balance those benefits and costs, please identify the disclosures that an entity should be required to include in its interim financial statements.

HP Response:

Fundamentally, we believe the disclosure requirements in the Revised Exposure Draft are excessive and will not provide users with meaningful information about the issuers of financial statements, as information required in the proposed disclosures is not consistent with information used by management in day to day operations. Additionally, we believe the significant costs associated with producing these interim and annual disclosures outweigh the benefits to users. Specifically:

- **We propose more reliance on information required by management and a re-assessment of the costs/benefits associated with the proposed disclosures.** The current proposed standards would require significant investment in gathering and presenting information that management would not routinely require for decisions and control. Additionally, the disclosures proposed would impose significant costs on the Company, both in terms of systems enhancements and integration efforts as well as the associated personnel-supported processes. For example, the costs to produce the detailed reconciliations will entail significantly more data capture than is now required by the Company, which will drive incremental costs in systems enhancements, maintenance and personnel to conduct the analyses required for these disclosures. HP does not believe these disclosures will provide users or analysts with useful information about the nature and direction of our business. We believe the significant costs to produce the proposed disclosures outweigh the benefit to users and analysts. For example, HP does not monitor or track information in a rollforward format for onerous performance obligations, contract assets, contract liabilities or capitalized costs for obtaining/fulfilling a contract, as it is not used by management in the decision making process. As an alternative, HP requests that the Boards place more reliance on information that Management deems useful in decision making and consider more principle-based disclosures. Not only would this provide more meaningful information to users and analysts about our business, it would also provide for greater cost savings.
- **Interim disclosure should be based on material changes.** HP requests that the Boards incorporate within the proposed standard on disclosures of revenue and contracts in interim financial reports, the concepts of “material changes” from the annual disclosures, similar to those outlined in the Security and Exchange Commission’s (SEC) Article 10 of Regulation S-X. We believe detailed information about revenue and contracts should be included when there is a material change in such detailed information as compared to that which was disclosed in the most recent fiscal year.

Question 6: Transfer of a non-financial asset that is not an output of an entity's ordinary activities.

Question 6: For the transfer of a non-financial 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 de-recognition 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?

HP Response: HP supports the adoption of a single standard, including the application to transfer nonfinancial assets that are not an output of our ordinary activities. However, as a company not routinely engaged in such transactions, and with the increase in estimates required for such transactions, we recommend that the standard retain the current guidance for Real Estate (included in ASC 360, *Property, Plant and Equipment*).

An entity's ability to reasonably and reliably estimate the transaction price may be significantly limited due to lack of sufficiently comparable transaction history with respect to non-financial assets, especially when such assets are not part of entity's ordinary activities.

Therefore, HP suggests that the Boards retain the existing guidance relative to Real Estate transactions and provide more examples for treatment of other non-financial assets as guidance for entities where such transactions are relatively rare.

Transition Guidance

We recognize, and support, the Boards proposal to provide meaningful information during transition to, and adoption of, the standards. As with significant changes recently adopted in accounting guidance (e.g., ASU No. 2009-13, *Multiple-Deliverable Revenue Arrangements* — a consensus of the FASB Emerging Issues Task Force ("ASU 2009-13"), ASU No. 2009-14, *Certain Revenue Arrangements That Include Software Elements* — a consensus of the FASB Emerging Issues Task Force ("ASU 2009-14")), we feel greater flexibility should be considered in the adoption of the standards, than that which is contained in the Revised Exposure Draft.

Retrospective adoption, particularly with the reassessment of existing contracts under the provisions of the new standard would, in effect, require duplicate sets of accounting processes and systems — given the detail anticipated in the standard. This reassessment would require revisions to estimates made at the outset of the arrangement, which would effectively re-characterize the nature of the arrangement.. The outcome of the previous accounting guidance compared to that provided in the Revised Exposure Draft would not reflect how the Company could instead chose to restructure ongoing arrangements to account for the new guidance, and therefore could be a misleading comparison.

Further, it would entail extensive systems investments, change management and potential re-characterization of prior earnings and tax obligations, including statutory adjustments where the impacts of these change may not be significant, in the aggregate. The modification to complex IT systems and tools used by entities will be considerable and entail significant ongoing maintenance expense. Such an approach should carefully weigh the costs and benefits of the proposal and one which we suggest may not rise to the expected usefulness contained in the Revised Exposure Draft. Based on the above, we strongly recommend the option for prospective adoption, with representative proforma statements of historical performance, where the proposed changes prove materially different to the company's historical results.

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The Company understands, and supports, the concepts of providing a sufficient period of historically comparable information for investors, analysts and users to make reasonable assessments of the company's performance over time and in the current reporting period. However, recent experience with the adoption of accounting changes in 2009 (ASU 2009-13/14, ASC 605-25), where such detailed comparisons were not suggested, led to no obvious distortion in the capital markets, among the investment and user community and had no other visible financial impacts.

Contract Costs

We request the Boards to revisit the requirement regarding capitalization of costs to acquire a contract, as described in paragraph 91. For example, with respect to sales commissions, there may be multiple models with varying criteria as to when the commission is earned. Additionally, commissions may be paid out at different times (quarterly, monthly, etc.). It will be difficult for entities to interpret the definition of an incremental cost consistently. Furthermore, we would be required to implement new systems, processes and controls in order to comply with this guidance. Given the materiality of commissions expense to many of our revenue-generating arrangements, we do not believe the cost outweighs the benefits for users of our financial statements. We do realize, however, that capitalization of these costs may be meaningful in some industries. Therefore, we recommend that an entity have the ability to make a policy election to either capitalize the costs or expense as incurred.

In summary, we support the general direction of the Proposed Accounting Standards Update (Revised)—*Revenue Recognition (Topic 605): Revenue from Contracts with Customers with the reservations stated above, and appreciate your consideration of our comments.*

If you have any questions regarding our views, please feel free to contact me at Jim.Murrin@hp.com

Sincerely,



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Senior Vice President, Controller, and Principal Accounting Officer