

Mr. Jackson M. Day
Technical Director
File Reference No. 2024-ED100
Financial Accounting Standards Board
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Proposed Accounting Standards Update, *Derivatives and Hedging (Topic 815)* and *Revenue from Contracts with Customers (Topic 606): Derivatives Scope Refinements and Scope Clarification for a Share-Based Payment from a Customer in a Revenue Contract* (File Reference No. 2024-ED100)

Dear Mr. Day:

We appreciate the opportunity to comment on the Proposed Accounting Standards Update, *Derivatives and Hedging (Topic 815)* and *Revenue from Contracts with Customers (Topic 606): Derivatives Scope Refinements and Scope Clarification for a Share-Based Payment from a Customer in a Revenue Contract* (the proposal), issued by the Financial Accounting Standards Board (FASB or Board).

We support the FASB's efforts to improve the guidance in Accounting Standards Codification (ASC or Codification) 815, *Derivatives and Hedging*, and clarify how to account for a share-based payment from a customer that is consideration for the transfer of goods or services under ASC 606, *Revenue from Contracts with Customers*, and other relevant accounting standards (e.g., ASC 815, ASC 321, *Investments – Equity Securities*).

We believe the FASB's proposal responds to many of the concerns raised by stakeholders about the complexity and cost of applying derivative accounting to certain types of contracts and about the diversity in practice that exists when accounting for a share-based payment from a customer that is consideration for the transfer of goods or services.

While we support the FASB's effort overall, there are certain aspects of the proposal that we believe the Board should reconsider, as well as areas that would benefit from additional clarification. These issues are addressed below and in Appendices A and B, which provide our responses to questions that the FASB included in the proposal.

Issue 1: Derivatives scope refinements

We support expanding the scope of contracts that would be excluded from derivative accounting. The current characteristic-based definition of a derivative under ASC 815 is broad, resulting in many types of contracts meeting the definition of a derivative and the need for companies to apply complex guidance in ASC 815 to determine whether they qualify for any scope exceptions. Some of these contracts have underlyings that are based on operations or activities specific to one of the parties to the contract. Stakeholders have said that applying derivative accounting to these contracts can be challenging and does not always provide decision-useful information to investors.

We believe the proposed scope exception would capture contracts for which it can be costly and challenging to apply the guidance in ASC 815 and for which derivative accounting may not always result in the best reflection of the economics of these arrangements in financial statements, as highlighted by stakeholders. These include contracts such as bonds with interest payments based on environmental, social and governance (ESG) metrics, research and development (R&D) funding arrangements, and litigation financing arrangements. We believe certain non-financial guarantee contracts and contingent consideration arrangements in asset acquisitions would also be excluded from derivative accounting, and we are supportive of this outcome.

We do, however, have concerns about the operability of the proposed predominant characteristics assessment that would need to be performed when a contract (or an embedded feature) contains multiple underlyings and only some of them qualify for a scope exception from derivative accounting. We note that the current correlation-based assessment is difficult to apply but believe the proposed fair value-based assessment would pose many of the same challenges, particularly when one underlying in a contract (or embedded feature) is dependent on another underlying being triggered (e.g., an interest rate swap that only becomes effective upon the successful completion of a business acquisition by one of the counterparties; commonly referred to as “deal contingent” swaps). In these situations, entities may need to engage valuation specialists to assist in the assessment, resulting in increased costs.

In addition, we expect the proposed scope exception would significantly increase the number of contracts (or embedded features) containing multiple underlyings that would be subject to the predominant characteristics assessment, but for which such an analysis is not currently required because none of the underlyings currently qualify for a scope exception from derivative accounting. A common example is a contingent redemption feature or conversion feature in debt instruments that becomes exercisable upon a change in control or an initial public offering (IPO) of the issuer. Under the proposal, these features would be subject to the predominant characteristics assessment, because one underlying (i.e., the occurrence of a change in control or an IPO) would qualify for a scope exception from derivative accounting, but the other underlying (i.e., the price of the bond or the price of the issuer’s common stock) would not.

Given the expected increase in number of contracts (or embedded features) that would be subject to the predominant characteristics assessment, coupled with the complexity of performing this assessment when one underlying is dependent on another underlying being triggered (which we believe would be fairly common in those contracts (or embedded features) that would become subject to the predominance assessment), we are concerned that the resultant costs of applying this assessment may not justify the financial statement reporting benefits of potentially excluding these contracts from the scope of derivative accounting.

In considering the potential benefits of the proposed amendments, we noted that for many of the contracts (or embedded features) that would become subject to the predominance assessment, relevant US GAAP guidance already exists to address the features in question, and we are not aware of diversity in practice with respect to the application of that guidance. For example, ASC 815 provides a four-step decision sequence that is applied to determine whether a contingent redemption feature should be bifurcated and accounted for as derivative. Similarly, ASC 815-40 provides comprehensive guidance on whether contingent conversion features (i.e., equity-linked features with contingent exercise provisions) should be bifurcated and accounted for as derivatives.

In our view, the alternative approach to eliminate the predominant characteristics assessment that was supported by some Board members would address these concerns. We believe that eliminating this assessment would generally not affect the application of the proposed scope exception to those contracts that were specifically identified by stakeholders as having led to the greatest amount of complexity and diversity in applying the definition of a derivative and related scope exceptions, which is the primary objective of this project.

We understand the concern raised by various Board members that removing the predominant characteristics assessment could theoretically result in a contract (or embedded feature) with multiple underlyings being accounted for as a derivative when it contains a nonqualifying underlying that is non-substantive or has a minimal impact on the overall contract (or embedded feature). To address this concern, we believe the Board could include language saying that non-substantive or minimal underlyings can be ignored when determining whether a contract (or embedded feature) would be excluded from the scope of derivative accounting.

Finally, we note that the scope of this project does not address the accounting for contracts (or embedded features) that would be excluded from derivative accounting as a result of the proposal. In paragraph BC15 of the proposal's Background Information and Basis for Conclusions, the Board observed that US GAAP includes guidance on how to account for many of the affected contracts. For example, ASC 730-20 provides guidance on accounting for R&D funding arrangements. We recommend the Board continue to monitor the application of existing US GAAP to affected contracts (e.g., R&D funding arrangements, litigation financing arrangements) to determine whether the financial reporting outcomes provide information that is useful to investors. If the financial reporting outcomes do not align with the underlying economics of affected contracts, then the Board should consider future standard setting (including through the Emerging Issues Task Force) to address those concerns.

Issue 2: Scope clarification for a share-based payment from a customer in a revenue contract

We also support clarifying the accounting by an entity that receives a share-based payment from a customer that is consideration for the transfer of goods or services. However, we believe the Board should further clarify certain language to improve the operability of the proposed guidance.

Please see Appendix A for our responses to the questions for respondents posed in the proposal. We provide other recommendations related to the proposal in Appendix B.

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We would be pleased to discuss our comments with the Board or its staff at their convenience.

Very truly yours,

Ernst & Young LLP

Appendix A – Responses to questions raised in the Proposed Accounting Standards Update, *Derivatives Scope Refinements and Scope Clarification for a Share-Based Payment from a Customer in a Revenue Contract*

Issue 1: Derivatives scope refinements

Question 1: Does the proposed scope exception in paragraph 815-10-15- 59(e) capture the population of contracts with entity-specific payment provisions that, in your view, should not be accounted for as a derivative and, instead, should be accounted for under other Topics? Conversely, does the proposed scope exception capture any types of contracts that, in your view, should continue to be accounted for as a derivative under Topic 815? Please explain why or why not. If not, what changes would you suggest?

We generally believe that the proposed scope exception in paragraph 815-10-15- 59(e) would capture the contracts with entity-specific payment provisions that, in our view, should not be accounted for as derivatives. Such contracts include bonds with interest payments based on ESG metrics, R&D funding arrangements, litigation financing arrangements, contingent consideration in asset acquisitions, programmatic loans and certain nonfinancial guarantees.

However, we believe certain other arrangements, such as guarantees provided by e-commerce platform companies to facilitate transactions on their platforms and monetization transactions that are economically similar to R&D funding arrangements, should also be excluded from derivative accounting.

Businesses conducted through e-commerce platforms have increased considerably in recent years. E-commerce platform companies provide a technical foundation or a set of applications and tools that other companies and their customers can use to conduct their day-to-day business activities. These platform companies may provide guarantees to platform participants (i.e., buyers and sellers of goods or services) to make sure there is an orderly facilitation of transactions on the platforms.

For example, a platform company may provide a performance guarantee to the buyer under which the platform company will make a payment to the buyer if the buyer is not satisfied with the goods (e.g., damaged, not up to the specifications agreed to) and the seller does not make the buyer whole. In this case, the underlying to the guarantee arrangement is the performance of the seller who is not a party to the guarantee arrangement between the platform company and the buyer. In addition, the platform company is not a party to the sale and purchase of goods between the seller and the buyer.

It is unclear to us whether such guarantee arrangements would be considered “contracts with entity-specific payment provisions” by the platform company and, therefore, meet the proposed scope exception in paragraph 815-10-15- 59(e) because the potential payment by the platform company relates to goods sold by the seller. However, given the platform's integral role in the business activities of the buyer and seller, enhancing their experiences is one of the business objectives of the platform company. We believe one reasonable interpretation would be that a guarantee of the performance of platform users, including buyers and sellers of goods and services provided by other companies, represents “operations or activities” specific to the platform company, and therefore, the

proposed scope exception in paragraph 815-10-15- 59(e) would apply. This outcome is consistent with our comment letter on the 2021 Invitation to Comment, *Agenda Consultation*, in which we said accounting for guarantees provided by platform companies for transactions that occur on the platform as derivatives may not result in the best financial reporting for those contracts.

Additionally, it is unclear whether the proposed scope exception would apply to transactions economically similar to the R&D funding arrangement illustrated in Case A of ASC 815-10-55-143A. A typical transaction involves a biotech company licensing its intellectual property (IP) to a larger pharmaceutical company, with variable consideration due from the pharmaceutical company to the biotech company that is linked to regulatory approval and/or royalties from the pharmaceutical company's commercialization of the IP. The biotech company separately enters into a transaction with a third-party investor in which it receives an upfront payment in exchange for all or a portion of the variable consideration it will receive in the future from the pharmaceutical company. The biotech company's involvement in the development of the licensed IP can vary from minimal participation to active collaboration. In this case, the underlying variable in the transaction with the third-party investor may be based on the Food and Drug Administration (FDA) approval of the IP that was licensed.

It is not clear in the proposal whether the biotech company would need to be actively involved in the development of the IP for the transaction with the third-party investor to qualify for the proposed scope exception. We believe one reasonable interpretation of the proposed guidance would be that the underlying variables to the payment provisions in the transaction with the third-party investor are considered "operations or activities of one of the parties to the contract," because the biotech company is the initial developer of the IP and a party to the licensing arrangement with the pharmaceutical company, which is an activity of the biotech company. Under that view the proposed scope exception would apply.

In addition, we agree with the proposal that the scope exception should not apply to variables based on a market rate, market price or market index because we generally believe contracts with such market-based underlyings are well understood to be derivatives and are not a source of diversity in practice. Similarly, we agree that the proposed scope exception should not apply to variables based on the price or performance of a financial asset or financial liability of one of the parties to the contract. However, as we discuss in our response to Question 2, we believe additional guidance is needed to clarify how broadly this concept could be applied.

While we generally agree with the Board's proposal to exclude from derivative accounting variables based on operations or activities specific to one of the parties to the contracts, we recognize that such a broad exception could result in contracts that were not explicitly identified by stakeholders as being a source of undue complexity or diversity potentially being excluded from the scope of derivative accounting pending the outcome of the proposed fair value-based predominant characteristic assessment. Examples of such contracts include deal-contingent interest rate swaps, contingently exercisable warrants and contingent redemption features settleable in shares. See further details in our responses to Questions 3 and 4.

Question 2: Is the proposed scope exception in paragraph 815-10-15-59(e) clear and operable? Please explain why or why not. If not, what changes would you suggest?

Overall, we believe that the proposed scope exception in paragraph 815-10-15-59(e) would be operable. However, we believe additional guidance is needed to further clarify what it means for an underlying to be “based on the operations or activities specific to one of the parties to the contract.”

The proposed guidance in paragraph 815-10-15-59(e) provides examples of events deemed to be specific to the operations or activities of one of the parties to the contract, such as obtaining regulatory approval, achieving a product development milestone or reaching a greenhouse gas emissions target. “Operations or activities specific to one of the parties to the contract” is not a defined term in the Codification and could be interpreted broadly. We are concerned that the lack of specificity or a clear principle could result in diversity in practice for certain types of contracts.

While we understand it may be difficult to articulate a principle that defines “operations or activities specific to one of the parties to the contract,” one way to address this would be by adding examples in the guidance, including those related to the e-commerce platform guarantees and monetization transactions by a biotech company as discussed in our response to Question 1.

Furthermore, including an example of a contract with an underlying based on the occurrence or nonoccurrence of an event that would not meet the proposed scope exception would also help stakeholders understand and apply the principle of “operations or activities specific to one of the parties to the contract.”

In addition, we believe it would be useful for the FASB to clarify the proposed guidance in paragraph ASC 815-10-15-59(e) that states, “(t)his scope exception does not apply to variables based on ... the price or performance (including default) of a financial asset or financial liability of one of the parties to the contract.” Based on the discussion in paragraph BC20 of the proposal’s Background Information and Basis for Conclusions, it’s clear that the Board did not intend to apply the scope exception to credit default swaps or broaden the scope exception that already exists for financial guarantees. However, it is not clear to what extent the Board intended to prohibit the scope exception beyond these instruments.

It is becoming more common for insurance companies to write “insurance-like products” that do not qualify as insurance contracts under ASC 944, *Financial Services – Insurance*, and, therefore, are generally accounted for as derivatives today. An example of such an arrangement is when an insurance company provides protection against a negative tax ruling on an uncertain tax position.

Another example is when a company that had initially won a judgment against a defendant in a lawsuit decides to execute a contract with an insurance company to “insure” against a negative outcome in the appellate court (sometimes referred to as judgment preservation insurance). The company will typically pay the insurance company a premium to buy this protection. The underlying in this contract (i.e., a negative outcome in the appellate court) could be viewed as the occurrence or nonoccurrence of an event related to “operations or activities specific to one of the parties to the contract” because it relates to litigation involving the company and a payout based on a favorable or

unfavorable outcome. However, one could also view this arrangement as the insurance company providing protection against a non-recognized financial asset of the company (the company would not recognize an asset associated with the initial judgment in its favor since this would be considered a gain contingency). That is, the arrangement could be viewed as having a variable based on the price or performance of a financial asset or financial liability of one of the parties to the contract, and thus, neither party would qualify for the scope exception.

We suggest the Board clarify its intent for these types of arrangements.

Question 3: Is the proposed predominant characteristics assessment in paragraph 815-10-15-60 operable, including for contracts with multiple underlyings that are dependent on each other? Please explain why or why not. If not, what changes would you suggest?

Question 4: The Board rejected an alternative to the proposed amendments to the predominant characteristics assessment in paragraph 815-10-15-60 that would have eliminated that assessment and replaced it with a requirement that if any underlying does not qualify for a scope exception in paragraph 815-10-15-59, the entire contract would not qualify for the scope exception (see paragraphs BC31 through BC32). Do you have any views on the alternative rejected by the Board and whether it would be more operable, be less complex, or provide more decision-useful information?

The proposed fair value-based predominant characteristics assessment may be more operable than the existing correlation-based assessment in relatively straightforward fact patterns, such as the one illustrated in Example 14B in the proposal. In that fact pattern, an entity enters into a pay-fixed, receive-variable interest rate swap, where the fixed leg of the swap is increased by 25 basis points if the entity fails to meet certain ESG targets, but the variable leg is not affected by this event. The example indicates that the entity could determine which of the two underlyings in the contract (i.e., the nonoccurrence of the entity achieving its ESG target or the variability in the interest rate index) is expected to have the largest effect on changes in the fair value of the contract by comparing the expected change in fair value of each underlying while holding the other constant.

However, we question whether such an approach could be applied when one of the underlyings in the contract (or embedded feature) is dependent on another underlying being triggered (e.g., a debt instrument with a put option that is only exercisable upon the occurrence of an IPO by the issuer). In such a fact pattern, the occurrence or nonoccurrence of an event (which represents one underlying) will ultimately result in either a zero payoff if the contingent event is not triggered or a payout that is based solely on the variability of the other underlying (e.g., the change in the price of the bond) if the required contingency is triggered.

We believe the proposed fair value-based assessment in this type of fact pattern would pose many of the same challenges that exist under the correlation-based assessment approach. We are concerned about the operability of the proposed predominant characteristics assessment, particularly when one underlying in a contract is dependent on another underlying being triggered.

We question whether the increased costs that would be incurred under the proposed model would justify the potential financial statement reporting benefits. In these situations, the proposal would seem to increase the complexity and cost associated with determining whether a contract is or is not included in the scope of ASC 815 as entities would be required to perform a predominant characteristic assessment for many contracts (or embedded features) where such an assessment is not currently required. This is because none of the underlyings currently qualify for a scope exception from derivative accounting. As discussed in our cover letter, in considering the potential benefits of the proposed amendments we noted that for many of the contracts (or embedded features) that would become subject to this assessment, relevant US GAAP guidance already exists to address the features in question, and we are not aware of diversity in practice with respect to the application of that guidance.

Therefore, we recommend that the Board reconsider the alternative approach to eliminate the predominant characteristics assessment that was supported by some Board members but ultimately rejected. Under this approach, a contract (or embedded feature) with multiple underlyings would only be excluded from derivative accounting if all of the underlyings qualified for a scope exception.

While this approach would be significantly less complex and costly to apply, it could result in certain contracts (or embedded features) that may have been excluded from derivative accounting pending the outcome of the proposed predominant characteristic assessment, continuing to be accounted for as derivatives. However, we generally believe that eliminating this assessment would not affect the application of the proposed scope exception to contracts that were specifically identified by stakeholders as having led to the greatest amount of complexity and diversity in applying the definition of a derivative and related scope exceptions.

In addition, to address the concern of certain Board members that removing the predominant characteristics assessment could result in a contract (or embedded feature) with multiple underlyings being accounted for as a derivative when it contains a nonqualifying underlying that is non-substantive or has a minimal impact to the overall contract (or embedded feature), we suggest that the Board provide guidance indicating that non-substantive or minimal underlyings can be ignored when determining whether a contract (or embedded feature) would be excluded from the scope of derivative accounting.

Question 5: Is the proposed transition method operable? If not, why not, and what transition method would be more appropriate and why? Would the proposed transition disclosure be decision useful? Please explain why or why not.

We believe the proposed transition method would be operable. We agree with providing entities the option to apply the proposal on a prospective basis or apply it to all affected contracts that exist as of the beginning of the fiscal year of adoption through a cumulative-effect adjustment to the opening balance of retained earnings (i.e., a modified retrospective approach). Given that some of the contracts that would be affected may be long dated in nature, we believe providing this flexibility in transition approaches would be warranted.

We also support the Board's proposal to provide entities with a one-time election to irrevocably apply the fair value option on an instrument-by-instrument basis to contracts that would no longer be accounted for as derivatives (or bifurcated embedded derivatives) upon transition, as long as the instruments meet the fair value option scope requirements in ASC 825, *Financial Instruments*.

While we understand that an entity could continue to account for these existing contracts as derivatives if it chooses to apply the proposed guidance prospectively, the ability to elect the fair value option for these instruments would result in greater consistency in presentation and disclosures between existing contracts and similar contracts executed by the entity after the date of adoption.

Question 7: Would the expected benefits of the proposed amendments justify the expected costs? If not, please describe the nature and magnitude of those costs, differentiating between one-time costs and recurring costs.

While we believe investors and preparers are in the best position to respond to this question, we have certain observations related to the cost-benefit analysis of the proposal for the FASB to consider.

We agree that expanding the scope of contracts to exclude from derivative accounting would reduce the cost and complexity for contracts that could be determined to no longer be under the scope of ASC 815 without the need for entities to perform a predominant characteristics assessment. This would include contracts (or embedded features) with a single underlying based on the operations or activities specific to one of the parties to the contract (e.g., many litigation financing arrangements), as well as those with multiple underlyings where the proposed scope exception would result in all of the underlyings qualifying for a scope exception (e.g., R&D funding arrangements with underlyings based on both FDA approval and royalties).

However, as discussed in our cover letter and our responses to Questions 3 and 4, we have concerns about whether the costs associated with the expected increase in the number of contracts (or embedded features) that would be subject to the predominant characteristic assessment justify the potential financial statement reporting benefits of the proposed amendments.

Issue 2: Scope clarification for a share-based payment from a customer in a revenue contract

Question 8: Do you agree that an entity should apply the guidance in Topic 606, including the guidance on noncash consideration in paragraphs 606-10-32-21 through 32-24, to a share-based payment from a customer that is consideration for the transfer of goods or services in a revenue contract? Do you agree that the share-based payment should be recognized as an asset under Topic 606 when an entity's right to receive or retain the share-based payment from a customer is no longer contingent on the satisfaction of a performance obligation? Please explain why or why not for both questions. If not, what changes would you suggest?

We agree that an entity should apply ASC 606, including the guidance on noncash consideration in ASC 606-10-32-21 through 32-24, to a share-based payment from a customer that is consideration for the transfer of goods or services in a revenue contract. However, we believe that a share-based payment may be recognized as an asset under ASC 606 (i.e., as a contract asset) before the entity's right to

receive or retain the share-based payment is no longer contingent on the satisfaction of a performance obligation. Further, we do not believe it was the Board's intent for an entity to apply either ASC 321 or ASC 815 to the share-based payment before the entity has an unconditional right to the share-based payment. Accordingly, we believe the FASB should make certain changes to the proposed language in paragraph 606-10-15-3A, as discussed below.

The proposal says, "... under this Topic, the share-based payment is recognized as an asset measured at the estimated fair value at contract inception when the entity's right to receive or retain the share-based payment from a customer is no longer contingent on the satisfaction of a performance obligation." However, under ASC 606, an entity may record an asset (i.e., a contract asset) before it has an unconditional right to receive or retain the share-based payment.

For example, an entity may satisfy a performance obligation (and, therefore, recognize revenue) before having an unconditional right to receive or retain the share-based payment. Its right may be conditional, for example, when an entity has to first satisfy another performance obligation in the contract before it is entitled to payment from the customer. In such cases, an entity would record a contract asset under ASC 606.

Proposed paragraph 606-10-15-3A also states, "The guidance in Topic 815 and Topic 321 does not apply to a share-based payment from a customer that is consideration for the transfer of goods or services unless and until the share-based payment is recognized as an asset under this Topic." As discussed above, there may be situations in which a contract asset (i.e., an asset recognized under ASC 606) is recognized before an entity has an unconditional right to receive or retain the share-based payment.

As mentioned above, we do not believe it was the Board's intent for an entity to apply either ASC 321 or ASC 815 to the share-based payment before the entity has an unconditional right to the share-based payment.

Further, we believe that other ASC topics may need to be considered when an entity receives a share-based payment from a customer that is consideration for the transfer of goods and services. For example, ASC 323, *Investments – Equity Method and Joint Ventures*, may be applicable in certain circumstances.

For these reasons, we recommend that the Board make the following changes (in bold and underscored) to ASC 606-10-15-3A:

606-10-15-3A An entity shall apply the guidance in this Topic, including the guidance on noncash consideration in paragraphs 606-10-32-21 through 32-24, to a contract with a share-based payment (for example, shares, share options, or other equity instruments) from a customer that is consideration for the transfer of goods or services. Accordingly, under this Topic, ~~an entity shall the share-based payment is recognized as an asset measured at the~~ **estimated fair value of the share-based payment** at contract inception **in order to determine the transaction price** ~~when the entity's right to receive or retain the share-based payment from a customer is no longer contingent on the satisfaction of a performance obligation.~~ The guidance in **other Topics (e.g., Topic 815, and Topic 321)** does not apply to a share-based

payment from a customer that is consideration for the transfer of goods or services unless and until **the entity has an unconditional right to receive or retain** the share-based payment ~~is recognized as an asset~~ under this Topic.

In Appendix B, we also suggest corresponding changes to Example 31 in ASC 606. Lastly, we believe that certain guidance proposed as additions by the Board to paragraph 606-10-15-3A and Example 31 (specifically new paragraph 606-10-55-250A) should also (or instead) be added to the guidance on noncash consideration guidance in ASC 606-10-32-21 through 32-24. This is because a user of the Codification is more accustomed to finding accounting guidance in the Recognition and Measurement sections of an ASC topic, rather than in Scope or Illustrations. Therefore, we propose the following **new** paragraph (in bold and underscored):

606-10-32-21A The guidance in other Topics (e.g., Topic 815, Topic 321) does not apply to a share-based payment from a customer that is consideration for the transfer of goods or services unless and until the entity has an unconditional right to receive or retain the share-based payment under this Topic. In situations in which an entity performs by transferring goods or services to a customer before or after the entity's right to receive or retain a share-based payment from the customer is unconditional, the entity should apply the guidance in Section 606-10-45.

Question 9: Should Topic 815 and Topic 321 be amended as proposed to clarify that the guidance in those Topics does not apply to a share-based payment from a customer that is consideration for the transfer of goods or services unless and until the share-based payment is recognized as an asset under Topic 606? Please explain why or why not. If not, what changes would you suggest?

We believe the FASB should amend ASC 321 and ASC 815 to clarify when the guidance in those topics would apply to a share-based payment from a customer that is consideration for the transfer of goods or services. We also believe the Board should further clarify its proposed language to more closely align to what we believe was its intent. That is, an entity should not apply the guidance in ASC 321 or ASC 815 to the share-based payment unless and until it has an unconditional right to the share-based payment under ASC 606.

We recommend that the Board make the following changes (in bold and underscored) to clarify the proposed guidance:

321-10-15-7 The guidance in this Topic does not apply to a share-based payment from a customer that is consideration for the transfer of goods or services unless and until **an entity has an unconditional right to receive or retain** the share-based payment ~~is recognized as an asset~~ under Topic 606 on revenue from contracts with customers.

815-10-25-16A The guidance in this Topic does not apply to a share-based payment from a customer that is consideration for the transfer of goods or services unless and until **an entity has an unconditional right to receive or retain** the share-based payment ~~is recognized as an asset~~ under Topic 606 on revenue from contracts with customers.

In addition, ASC 815-10-25-5(e), as proposed, could indicate that any and all share-based payments (e.g., warrants, shares) within a revenue contract would be addressed in the recognition section of ASC 815. We believe the Board's intent was for this guidance to apply only to a share-based payment received as consideration for the transfer of goods and services to a customer in a revenue contract. For example, it would not apply to an entity's purchase of shares from a customer that may be included in a revenue contract. Therefore, the draft wording in this paragraph may result in unintended consequences.

We recommend that the Board make the following changes (in bold and underscored) to clarify the proposed guidance:

815-10-25-5

e. A share-based payment received from a customer as consideration for the transfer of goods or services in a revenue contract that is within the scope of Topic 606.

Question 10: Are the proposed amendments clear and operable? Please explain why or why not. If not, what changes would you suggest?

Refer to our responses to Questions 8 and 9 for suggested changes to clarify the proposed amendments and make them more operable. We also include some additional suggestions below for improving the clarity and operability of the proposal.

An entity that has an unconditional right to noncash consideration (e.g., a share-based payment that is received as consideration for the transfer of goods and services) would recognize a receivable in accordance with ASC 606-10-45-4. However, such receivable (e.g., a right to receive a share-based payment) may be accounted for in accordance with ASC topics other than ASC 310 and ASC 326-20 (e.g., ASC 815). Accordingly, we recommend that the Board make the following changes (in bold and underscored) to clarify ASC 606-10-45-4:

606-10-45-4 A receivable is an entity's right to consideration that is unconditional. A right to consideration is unconditional if only the passage of time is required before payment of that consideration is due. For example, an entity would recognize a receivable if it has a present right to payment even though that amount may be subject to refund in the future. An entity shall account for a receivable in accordance with other Topics (e.g., Topic 310, and Subtopic 326-20). Upon initial recognition of a receivable from a contract with a customer, any difference between the measurement of the receivable in accordance with Subtopic 326-20 and the corresponding amount of revenue recognized shall be presented as a credit loss expense.

In addition, while the Board scoped this issue narrowly (i.e., noncash consideration received in the form of a share-based payment only), there are similar situations for which there is a lack of guidance. One example is when an entity receives other forms of noncash consideration for the transfer of goods or services to a customer (e.g., property, plant and equipment; crypto assets).

We expect that entities may try to analogize to this guidance for other forms of noncash consideration received. If the Board does not believe this would be appropriate, the final guidance should clarify that fact. Alternatively, the Board could consider clarifying whether the pending content can be applied more broadly to noncash consideration of all forms (potentially in the Basis for Conclusions section of the final ASU).

Lastly, an entity may receive a share-based payment from a vendor that is in the scope of ASC 705-20, *Cost of Sales and Services – Accounting for Consideration Received from a Vendor*. There is a lack of clarity about how an entity should account for the share-based payments received from a vendor.

For example, if an entity receives share-based payments from a vendor that are contingent on certain conditions being met by the entity, it is unclear whether the share-based payments should (1) be recognized at contract inception in accordance with ASC topics other than ASC 705-20 (e.g., as a derivative asset under ASC 815 or an equity security under ASC 321), or (2) should not be recognized until the entity satisfies the conditions under ASC 705-20. Therefore, we recommend the Board consider clarifying the accounting of a share-based payment received from a vendor that is in the scope of ASC 705-20 in a future project.

Question 11: Subtopic 610-20, Other Income—Gains and Losses from the Derecognition of Nonfinancial Assets, refers to the revenue recognition principles in Topic 606, including the recognition and measurement guidance. Should the scope of Subtopic 610-20 be amended to be consistent with the proposed clarification in Topic 606? That is, should the Board clarify that a share-based payment from a noncustomer that is consideration for the transfer of a nonfinancial asset (that is within the scope of Subtopic 610-20) should be accounted for under Subtopic 610-20? Please explain why or why not. Do you expect any unintended consequences of providing that clarification? If so, please explain what those unintended consequences would be.

We believe the scope of ASC 610-20 should be amended to be consistent with the proposed clarification in the Scope section of ASC 606. While ASC 610-20 refers to various components of ASC 606, it only specifically refers to paragraph 606-10-15-4 of ASC 606's scoping guidance. However, even if this change to ASC 610-20's scope is not made, we believe that an entity would likely apply the guidance in ASC 606 by analogy when a share-based payment is received from a noncustomer in consideration for the transfer of a nonfinancial asset that is in the scope of ASC 610-20. However, amending ASC 610-20 would clarify the Board's intent and could eliminate any potential diversity in practice. In addition, we do not expect any unintended consequences of providing such clarification.

However, if the Board makes our proposed edit to the guidance on noncash consideration in ASC 606 that we include in our response to Question 8 (i.e., by adding new paragraph ASC 606-10-32-21A), and because ASC 610-20-32-3 specifically refers to the noncash consideration guidance in ASC 606, we believe a change to ASC 610-20's scoping guidance would be unnecessary.

Question 12: Is the proposed transition method operable? If not, why not, and what transition method would be more appropriate and why? Would the proposed transition disclosures be decision useful? Please explain why or why not.

While we believe the proposed transition method would be operable, it is unclear why the transition methods for Issues 1 and 2 would be different.

For Issue 1, the guidance would be applied prospectively to new contracts, with the option to apply it to contracts that exist as of the beginning of the fiscal year of adoption through a cumulative effect adjustment. For Issue 2, entities would be required to apply the guidance to existing revenue contracts as of the beginning of the fiscal year of adoption. That is, prospective adoption would not be an option, and this would increase transition-related costs for all entities. It's not clear whether these incremental costs would outweigh any benefits received by users of this additional information.

Appendix B – Other comments

As discussed in our response to Question 8, we suggest the following changes (in bold and underscored) to Example 31 in ASC 606 to clarify the proposed guidance. We suggest reordering some of the discussion in the example to focus on the ASC 606 accounting first, as well as implement similar changes as previously discussed. The changes tracked are from the proposed version, not from Example 31 as currently included in the Codification:

Example 31–Entitlement to Noncash Consideration

606-10-55-248 An entity enters into a contract with a customer to provide a weekly service for one year. The contract is signed on January 1, 20X1, and work begins immediately. In exchange for the service, the customer promises 100 shares of its common stock per week of service (a total of 5,200 shares for the contract). The terms in the contract require that the shares must be paid upon the successful completion of each week of service.

606-10-55-249 In accordance with paragraph 606-10-15-3A, the entity applies the guidance in this Topic to a contract with a share-based payment from a customer that is consideration for the transfer of a service (the shares). ~~The entity concludes that its right to receive 100 shares from the customer is no longer contingent on its performance once it completes each week of service. As a result, the 100 shares are recognized as assets under this Topic as each week of service is complete. In this Example, the timing of the recognition of the shares coincides with the timing of the payment of the shares. The guidance in other Topics does not apply to the shares until the shares are recognized as assets under this Topic.~~ **[Content moved to paragraph 606-10-55-250A]** The entity concludes that the service is a single performance obligation in accordance with paragraph 606-10-25-14(b). This is because the entity is providing a series of distinct services that are substantially the same and have the same pattern of transfer (the services transfer to the customer over time and use the same method to measure progress—that is, a time-based measure of progress).

606-10-55-250 To determine the transaction price (and the amount of revenue to be recognized), the entity measures the estimated fair value of 5,200 shares at contract inception (that is, on January 1, 20X1) in accordance with paragraph 606-10-32-21. The entity measures its progress toward complete satisfaction of the performance obligation and recognizes revenue ~~and the corresponding 100 shares (measured at the estimated fair value at contract inception)~~ **equal to 1/52 of the estimated fair value of the 5,200 shares** as each week of service is complete. The entity does not reflect any changes in the fair value of the 5,200 shares after contract inception in the transaction price in accordance with paragraph 606-10-32-23.

606-10-55-250A The entity concludes that its right to receive 100 shares from the customer is ~~no longer contingent on its performance~~ **unconditional** once it completes each week of service. As a result, the entity looks to other Topics (e.g., Topic 321) to determine how to account for the 100 shares ~~are recognized as assets under this Topic~~ **received** as each week of service is complete. In this Example, the timing of the recognition of the shares coincides

with the timing of the payment of the shares. The guidance in other Topics does not apply to the shares unless and until the entity has an unconditional right to receive or retain the shares ~~are recognized as assets~~ under this Topic. **[Content moved from paragraph 606-10-55-249 and edited.]** Once the 100 shares are recognized under ~~this other~~ Topics ~~as each week of service is complete~~, the entity then applies the guidance in those other Topics to determine whether and how any changes in fair value that occurred after contract inception due to the form of the noncash consideration should be recognized and presented in accordance with paragraph 606-10-32-23.

606-10-55-250AB In situations in which an entity performs by transferring goods or services to a customer before or after the entity's right to receive or retain a share-based payment from the customer is ~~no longer contingent on the satisfaction of a performance obligation~~ unconditional, the entity should apply the guidance in Section 606-10-45. **[Alternatively, this paragraph could be removed entirely and included in new paragraph 606-10-32-21A as shown above in our response to Question 8.]**