

October 21st, 2024

Mr. Jackson Day
Technical Director
Financial Accounting Standards Board
801 Main Avenue
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Norwalk, CT 06856-5116

By email: director@fasb.org

RE: File Reference No. 2024-ED100, Derivatives Scope Refinements and Scope Clarification for a Share-Based Payment from a Customer in a Revenue Contract

Dear Mr. Day,

The International Swaps and Derivatives Association's ("ISDA")¹ Accounting Policy Committee (the "Committee") appreciates the opportunity to comment and provide feedback on the Financial Accounting Standards Board's ("FASB" or "Board") Proposed Accounting Standards Update, *Derivatives and Hedging (Topic 815) and Revenue from Contracts with Customers (Topic 606)* (the "Proposed ASU" or "Exposure Draft"). Collectively, the Committee members have substantial professional and practical expertise addressing accounting policy issues related to financial instruments.

The Committee appreciates your consideration of this topic and thanks you for providing the proposed reporting guidelines and clarifications to address questions that have been raised by stakeholders. The Committee supports the FASB's proposals in the Exposure Draft and believes that the Exposure Draft will improve the application and relevance of the Derivatives and Hedging (Topic 815) and Revenue from Contracts with Customers (Topic 606) guidance, and we have provided comments below reflecting further potential refinements and improvements to this guidance for the Board's consideration. The examples and guidance in the Exposure Draft address the issues found in the application of the existing derivatives guidance to contracts with underlyings that are specific to one of the parties to the contract. The Committee has discussed the questions for respondents provided by the Board and our feedback is included below.

Questions for Respondents

Issue 1: Derivative 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

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as a derivative under Topic 815? Please explain why or why not. If not, what changes would you suggest?

The Committee believes the proposed scope exception in ASC 815-10-15-59(e) generally captures the population of contracts with entity-specific payment provisions that should be excluded from the scope of derivative accounting, but as discussed below, we believe there is risk that the proposed scope exception could be interpreted and applied more narrowly than the Board may have intended. Specifically, ASC 815-10-15-59(e)(1) indicates that the scope exception applies to contracts with underlyings that are based on the financial statement metrics of one of the parties to the contract. There will be instances where a contract may reference a financial metric that is not explicitly included in or derived from an entity's financial statements, such as regulatory metrics (e.g., regulatory capital measurements) or non-financial metrics such as environmental, social and governance ("ESG") items (e.g., carbon emissions). The Committee believes the Board may not have intended to exclude such underlyings from qualifying for the scope exception, and suggests revising the example in ASC 815-10-15-59(e)(1), as follows:

1. ~~The financial statement M~~etrics of one of the parties to the contract. ~~The financial statement S~~uch metrics include metrics derived from amounts presented in financial statements, regulatory reports, components of amounts included in ~~financial~~ those statements and reports, or other financial or non-financial metrics that are specific to one of the parties to the contract (for example, earnings before interest, taxes, return on tangible equity, carbon emissions or board diversity/composition/representation) ~~depreciation, and amortization; net income; expenses; or total equity of one of the parties to the contract~~).

The Committee also suggests providing additional guidance related to distinguishing between entity-specific metrics and market-based variables. As currently written, ASC 815-10-15-59(e)(2) states "This scope exception does not apply to variables based on a market rate, market price, or market index." The Committee suggests clarifying that a market-based underlying would not be precluded from qualifying for the scope exception, provided there is an element of the metric that is specific to the entity.

We do not believe it was the FASB's intent for the two examples included in ASC 815-10-15-59(e) – financial statement metrics or the occurrence or non-occurrence of an event – to be all inclusive. As such, the Committee asks the Board to explicitly state that the list of examples is not intended to be an all-inclusive list of features that meet the scope exception. This would avoid potential diversity in interpretation or practice when assessing whether an underlying qualifies for the scope exception demonstrated in ASC 815-10-15-59(e). Specifically, the Committee proposes the following:

- e. A variable that is based on operations or activities specific to one of the parties to the contract. An underlying would not be precluded from qualifying for the scope exception if the metric is market based, provided there is an element of the metric that is specific to a party to the contract. ~~For example, this scope exception applies to contracts with underlyings based on the following:~~ Examples of contracts containing underlyings that meet the scope exception include but are not limited to: ...

Clarifying that the examples are not an all-inclusive list will allow more consistent application of the guidance to a broader range of entity-specific activities. Further, such a clarification will preclude any views that future standard-setting activities would be required add additional underlyings to a specified qualifying list.

Additionally, under Example 13, the term "financial variable" is introduced. While the guidance provides examples of physical variables (e.g., climatic or geological variables), the term "financial variable" is not adequately defined, which may lead to misapplication of the guidance. The Committee suggests aligning the definition of a financial variable to the characteristics of a financial instrument. The definition of a financial

instrument requires a chain of contractual obligations that ends with the delivery of cash or an ownership interest in an entity.

The Committee also believes there could be scoping assessment issues under ASC 815-10-15-59(e)(2) specific to certain contracts with contingent payment features, such as deal contingent swaps. Under a deal contingent swap, a purchasing entity enters into an interest rate swap that is cancelled if the deal is not executed. The deal contingent underlying relates to the occurrence or nonoccurrence of an event that is specific to one of the parties to the contract (e.g., the purchasing party making the acquisition). A second underlying is the interest rate variable on the swap.

The deal contingency means the swap will be cancelled and have no value if the deal is not consummated. The potential fair value impact of the interest rate variable is dependent on deal contingency being resolved. As a result, the two underlyings are inherently inter-related, and it is operationally difficult and not practicable to evaluate each underlying independently of the other.

To address this complexity and avoid the potential for diversity in practice, the Committee recommends that the guidance should be modified to treat such inter-related underlyings as a single underlying. Under this approach, the deal contingency and the interest rate underlying would be assessed under this scope exception as a single underlying. If either component of this single underlying does not meet the scope exception criteria in ASC 815-10-59(e), the entire underlying does not meet the scope exception.

We suggest the following changes to the scoping paragraph under ASC 815-10-59(e)(2) to help preparers navigate the complex instruments and ensure consistent application of the guidance:

When evaluating whether operations or activities are specific to one of the parties to the contract, an entity does not need to consider whether the outcome is within its control. Additionally, if there are multiple underlyings that are inter-related, they should be analyzed as a single underlying. If any individual component of the inter-related underlyings does not meet the scope exception in this paragraph, the combined underlying would not be considered specific to a party to the contract. This scope exception does not apply to variables based on a market rate, market price, or market index (including those in paragraph 815-10-15-88(a) through (f)) or the price or performance (including default) of a financial asset or financial liability of one of the parties to the contract. For purposes of applying the scope exception in this paragraph, the term party to the contract refers to any entity within a consolidated group. (See Example 14A [paragraphs 815-10-55-143A through 55-143E].)

Finally, the Committee believes the Board should provide a practical expedient that permits an entity, on an instrument-by-instrument basis, to avoid having to perform a predominant characteristics assessment and instead elect to apply derivative accounting to a contract that has at least one underlying that does not meet the scope exception, but otherwise meets the definition of a derivative. Such a practical expedient would be consistent with the above proposed treatment of contracts with inter-related underlyings and significantly reduce operational burden and complexity of performing a predominance test.

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?

Refer to the Committee's response to Question 1. We believe if those matters are addressed, identifying features in the scope exception in ASC 815-10-15-59(e) will be clear and operable, thus providing sufficient guidance related to the initial recognition of these contracts.

However, the Committee believes the Board should provide certain guidance with respect to the subsequent accounting for instruments with underlyings that meet the scope exception in ASC 815-10-15-59(e).

Specifically, absent any other guidance, it appears that pursuant to ASC 320-10-30-40(b), many contracts that have entity-specific underlyings that qualify for the scope exception will be required to apply the retrospective interest method, which is required for notes that have a return on investment subject to variability (other than due to credit rating changes of a borrower) because of either of the following:

1. There is no stated coupon rate or the stated coupon is not fixed or prespecified, and the variation in the return on investment or coupon rate is not a constant percentage of, or in the same direction as, changes in market-based interest rates or interest rate index, for example, the U.S. Treasury Bill Index.
2. The variable or fixed coupon rate is below market rates of interest for traditional notes of comparable maturity and a portion of the potential yield (for example, upside potential for principal) is based on the occurrence of future events or circumstances. (Examples of instruments that meet this condition include inverse floating-rate notes, dual-index floating notes, and equity-linked bear notes.)

Under the retrospective approach, a new effective interest rate is determined each period based on the original carrying amount, actual cash flows to date and the remaining estimated cash flows. The new effective interest rate is then used to adjust the carrying amount to the present value of the revised estimated cashflows, discounted at the new effective interest rate.

Requiring entities to adjust the carrying values of contracts based on changes in the present value of estimated cash flows counteracts the simplification improvements created by this ASU. As noted in the Basis for Conclusions, accounting for these contracts as derivatives does not provide decision-useful information and creates complexity in the accounting for these instruments. The Committee believes application of the retrospective interest method, which subjects instruments to remeasurement based on changes in the present value of future cash flows, also does not provide decision-useful information to users of the financial statements and creates complexity and unnecessary costs and burdens on preparers.

As a result, the Committee requests that the Board provide an exception from applying the retrospective interest method to contracts that have potential variability in future interest rates solely due to features that meet the scope exception in ASC 815-10-15-59(e). Such an exception would address the above concerns and also align with the objectives of the Proposed ASU to address stakeholder concerns about having to apply a complex accounting model (i.e., derivatives) to certain contracts.

In other words, exempting certain contracts from derivative accounting under the Proposed ASU, to only instead require the application of a complex and potentially volatile interest recognition model, will likely not address or alleviate stakeholder concerns and entities would therefore be likely to continue to avoid such contracts and activities.

The Committee believes that contracts that qualify for the scope exception should be accounted for in a manner similar to variable rate instruments, for which the accrual of interest is prospectively adjusted on each rate reset date.

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?

Predominant Characteristics Assessment

The Committee believes the predominant characteristics assessment described in ASC 815-10-15-60 is operable and an appropriate method for determining whether an underlying, and therefore a contract, qualifies for the scope exception.

However, we believe there are specific areas where the proposed guidance could be modified to reduce the operational burden and provide additional clarity in its implementation without affecting the accounting conclusions. The Committee suggests the following changes to the proposed predominance test.

First, allowing a qualitative assessment in certain circumstances would significantly reduce the operational burden to perform a predominance assessment for every contract with multiple underlyings, and be better aligned with the Board's intent to reduce the cost and complexity of evaluating whether these contracts are derivatives. We suggest the Board allow entities to perform a qualitative assessment when it is clear that one underlying will have the greater expected effect on fair value. This would be consistent with other areas of the guidance which allow for such qualitative considerations. For example, ASC 470-20-40-9 provides for several considerations when determining whether a conversion option is substantive, including one criterion that includes a qualitative evaluation of the conversion options, such as the nature of the conditions under which the instrument may become convertible.

If a qualitative assessment does not provide a conclusive result, a quantitative assessment may then be performed. This approach would reduce unnecessary complexity and effort while still maintaining an assessment process. For example, a company enters into an interest rate swap with a fixed leg of 4% and a floating leg of SOFR, and the fixed leg will increase by 25 basis points if the company does not meet a specified emissions reduction target. Without performing a quantitative predominance characteristic assessment, it is clear that the interest rate underlying would be the predominant underlying, given the limited potential impact of the entity-specific underlying.

Second, if a contract has multiple underlyings that are inter-related (as discussed above), the predominant characteristics assessment should not be required between those underlyings. For example, when one underlying depends on another (e.g., a regulatory approval followed by sales targets of the approved product), the underlyings should be considered as a single underlying. Determining the change in fair value of one underlying that is dependent on another underlying can create significant valuation complexity and it may not be practicable to assess each underlying independently. Assessing these inter-related underlyings as a single underlying would reduce the operational burden for the number of assessments that need to be performed and reduce the complexity when applying this guidance. This recommendation aligns with the recommendation to consider inter-related underlyings as a single underlying when applying the scoping guidance, as described under Question 1. For purposes of assessing whether an inter-related underlying meets the scope exception under ASC 815-10-59(e), the inter-related underlyings are treated as one and if any component of the underlying does not meet the scope exception the entire underlying does not meet the scope exception.

To implement the two suggestions above, we propose the following changes to ASC 815-10-15-60:

815-10-15-60: If a contract has more than one underlying and some, but not all, of them qualify for one of the scope exceptions in paragraph 815-10-15-59, the application of this Subtopic to that contract depends on its predominant characteristics. However, if the multiple underlyings in the contract are inter-related, these underlyings are assessed as a single underlying when performing the predominance characteristic assessment. When performing the predominant characteristics

assessment, making this evaluation, a qualitative or quantitative assessment may be performed. If the underlying(s) that do not meet the criteria for a scope exception ASC 815-10-15-59(e) are deemed to be non-substantive, the contract meets the scope exception. Otherwise, a quantitative predominance assessment is performed. When making this evaluation, the contract is eligible for a scope exception in accordance with paragraph 815-10-15-59 if the underlying that has the largest expected effect on changes in the fair value of the contract qualifies for a scope exception in accordance with paragraph 815-10-15-59.

Third, when performing the predominant characteristics assessment, paragraph 815-10-55-64 indicates that all “reasonably possible” changes in fair value should be considered. The Committee believes the “reasonably possible” requirement can create significant operational burden to potentially evaluate a wide range of scenarios. Contracts between two unrelated parties are typically executed based on expectations of likely scenarios, rather than improbable circumstances. Therefore, the term “more likely than not” may better reflect the reality that parties enter contracts with the anticipation of probable outcomes that will affect the contract’s fair value. By using “more likely than not” instead of “reasonably possible,” the assessment will better align with the expectations and intent of the parties involved to a contract and reduce operational burden. Further, to reduce the operational burden of identifying every possible scenario, we believe the guidance should indicate that this assessment is not intended to be exhaustive. There are other areas of the guidance which do not require every possible scenario to be considered. For example, in ASC 820-10-35-5A when identifying the principal market for fair value measurement a reporting entity is not required to undertake an exhaustive search for the principal market. Clarifying this is does not require every possible scenario to be considered will allow companies to implement this guidance without undue costs or operational burden.

Specifically, the Committee proposes the following change:

1. 815-10-55-64 Paragraph 815-10-15-60 requires that an entity perform the predominant characteristics assessment if a contract has more than one underlying and some, but not all, of them qualify for one of the scope exceptions in paragraph 815-10-15-59. Paragraph 815-10-15-60 also requires that an entity assess which underlying has the largest expected effect on changes in the fair value of the contract. When performing the assessment, the entity should consider all ~~reasonably possible~~ more likely than not changes in fair value. A reporting entity need not perform an exhaustive analysis of all possible scenarios.

This update with emphasis on “more likely than not” better aligns with the expectations of the parties entering into contracts, reduces the operational burden, and provides a clearer framework for evaluating the predominant characteristics of a contract.

Implementation Guidance:

The Committee agrees there is a need to provide illustrative examples to support preparers with the adoption and implementation of the predominant characteristics assessment. However, there are a few proposed edits across the different examples provided in ASC 815-10-55 to clarify the application for preparers and support consistent adoption of the guidance.

Case A: Underlyings Based on the Occurrence of Regulatory Approval and Achieving a Financial Statement Target

The Committee agrees with the Board’s analysis in ASC 815-10-55-143B that both underlyings in Case A (FDA approval and sales exceeding \$500 million) qualify for the scope exception. However, as noted above, when performing the predominant characteristics assessment, we suggest evaluating the two interrelated underlyings as a single underlying. This example would illustrate that because both underlyings are dependent on FDA approval, and such approval is specific to one party to the contract, the scope exception

would be met. This clarification would make it clear that no additional analysis is necessary for interrelated underlyings that are within the scope exception.

If the Board does not incorporate the proposal to assess inter-related underlyings as one underlying, we propose clarifying that no predominant characteristics assessment is required when all underlyings either qualify for the scope exception or do not. For the avoidance of doubt, updating the example to explicitly state that when both underlyings qualify for the scope exception, the test would not be required to be performed:

ASC 815-10-55-143C: Therefore, those two underlyings each qualify for the scope exception in paragraph 815-10-15-59(e) and no predominant characteristics assessment is required to be performed.

Case B: Underlying Based on the Occurrence of an Initial Public Offering (IPO)

The example in ASC 815-10-55-143D includes a contingently puttable bond at \$102. This feature would be analyzed under the four-step model in ASC 815-15-25-42. Under this example, the amount paid upon settlement is not adjusted based on changes in an index and does not involve a substantial premium. Therefore, the embedded derivative would not need to be assessed whether this feature meets the scope exception.

As commented on above, ASC 815-10-15-60, 55-64 and Example 14B require comparing the largest expected effect of the underlying on a feature's fair value, considering all reasonably possible changes over the contract's life. In ASC 815-10-55-143D Case B, an IPO underlying has minimal impact on the put feature's value, as a note puttable at par (issued at market) holds little value to the holder. However, the put becomes more valuable if the security price drops due to rising interest rates or credit risk (security price underlying). We suggest modifying the example to a note puttable at a substantial premium (e.g., 150% of par) and clarifying events like an IPO may be more impactful than security price underlying, because considering all reasonable expectations, an IPO is more likely to occur than an extremely high interest/credit risk scenario.

Alternatively, the example could be changed to view security price and IPO as one unit of account, therefore precluding the need for performing the predominant characteristic test. Such view could be supported because the realization of the intrinsic value of the put is as a function of the then security price which would be impossible to realize without the occurrence of an IPO first.

The Committee believes Case B should be adjusted because it involves an embedded put feature that is clearly and closely related to the host contract and would not require bifurcation. Alternatively, if there are no changes made to the example, we suggest removing this example to avoid confusion.

Case C: Underlying Based on the Nonoccurrence of Achieving a Greenhouse Gas Emissions Reduction Target

As noted above, the Committee suggests allowing both a qualitative and quantitative approach when performing the predominant characteristics assessment. If this change is adopted by the Board, the Committee also recommends illustrating this approach in ASC 815-10-55-143H.

815-10-55-143H The contract is subject to the predominant characteristics assessment in paragraph 815-10-15-60 because it has two underlyings and one (the nonoccurrence of Entity A achieving a specified greenhouse gas emissions reduction target), but not both, of the underlyings qualifies for the scope exception in paragraph 815-10-15-59. When performing the predominant characteristics assessment, Entity A could decide to initially perform a qualitative assessment. In this example, because the increase in the fixed rate of the swap is 25 basis points, but interest is currently 5%, the company could qualitatively determine changes in interest rates is the predominant underlying. Alternatively, when performing a quantitative assessment, determining how to perform a fair value

assessment is a matter of judgment that depends on the relevant facts and circumstances. Entity A determines which underlying is expected to have the larger effect on changes in the fair value of the contract. Specifically, Entity A computes how much the fair value of the contract moves if the interest rate underlying changes over the life of the contract while keeping the greenhouse gas emissions reduction target underlying constant. Entity A then performs the same assessment for the greenhouse gas emission reduction target underlying while keeping the interest rate underlying constant. Entity A compares the results of the two assessments and determines that the interest rate underlying has the larger expected effect on changes in the fair value of the contract. Because the interest rate underlying is the predominant underlying and does not qualify for any of the scope exceptions in paragraph 815-10-15-59, Entity A concludes that the interest rate swap should be accounted for as a derivative under Topic 815.

This modification would highlight the ability to use both qualitative or quantitative method and reach the same conclusion.

ASC 815-10-55-143L provides an alternative conclusion under Case C where the company determines the greenhouse gas emissions is the predominant underlying. The Committee believes that this example is unrealistic, because the ESG feature triggers a 25-basis point adjustment that would effectively never be the predominant characteristic in a contract involving a plain vanilla interest rate swap. It is unclear how qualitatively or quantitatively such conclusion could be reached. Further, this example contradicts the existing guidance in ASC 815-15-25-9 which prohibits separating a compounded derivative into components that would be accounted for separately:

ASC 815-15-25-9 If a compound embedded derivative comprises multiple embedded derivative features that all involve the same risk exposure (for example, the risk of changes in market interest rates, the creditworthiness of the obligor, or foreign currency exchange rates), but those embedded derivative features differ from one another by including or excluding optionality or by including a different optionality exposure, an entity shall not separate that compound embedded derivative into components that would be accounted for separately.

Therefore, the Committee suggests the Board either remove this alternative conclusion or present a new fact pattern for this example.

Next, in reviewing Paragraph 815-10-55-143E, Example 14A, Case C, we noted that the interest rate adjustment is incorrectly referred to as an underlying. The interest rate adjustment is a contractual outcome triggered by the nonoccurrence of the greenhouse gas emissions reduction target, which is the actual underlying. To avoid confusion, we recommend removing the reference to the interest rate adjustment as an underlying in the last sentence of the paragraph. We would propose the following changes to Paragraph 815-10-55-143E:

1. 815-10-55-143E On July 1, 20X1, Entity A issues a five-year fixed-rate bond. If Entity A's parent entity, Parent A, fails to meet a specified greenhouse gas emissions reduction target at its consolidated group level by June 30, 20X3, the fixed interest rate on Entity A's bond increases by 0.25 percent for the remaining term. The bond is a hybrid instrument that contains an embedded feature (that is, the interest rate adjustment) that is required to be evaluated for bifurcation. Because Entity A is a subsidiary of Parent A, the nonoccurrence of Parent A achieving Parent A's consolidated greenhouse gas emissions reduction target is considered an activity specific to one of the parties to the contract for the purposes of both Entity A's standalone financial statements and Parent A's consolidated financial statements. The embedded feature is not based on a market rate, market price, or market index or the price or performance of a financial asset or financial liability of one of the parties to the contract. Therefore, the nonoccurrence of the greenhouse gas emissions

~~reduction target interest rate adjustment~~ underlying qualifies for the scope exception in paragraph 815-10-15-59(e).

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?

If the proposed recommendations described above are adopted, the Committee believes the Proposed ASU would achieve the Board's objective to address stakeholder concerns around the application of derivative accounting to contracts with features based on operations of one of the parties to the contract. The Committee is supportive of the current approach as it will mitigate the stakeholder concerns around the type of features in-scope of the scope exception in ASC 815-10-15-59(e).

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.

The Committee believes the proposed guidance in ASC 815-10-15-60 is operable but would benefit from the adoption of the above suggested changes. The Committee agrees with the transition requirement that gives entities the ability to elect to apply the proposed amendments using either a prospective approach or a retrospective approach.

Question 6: In evaluating the effective date, how much time would be needed to implement the proposed amendments? Should the effective date for entities other than public business entities be different from the effective date for public business entities? Please explain why or why not.

In evaluating of the effective date, the Committee believes that the proposed amendments should be effective for annual and interim periods beginning one year after the publication of the ASU, and no distinction should be made between public business entities and entities other than public business entities. In addition, we believe that early adoption should be permitted in any interim or annual periods in which financial statements have not yet been issued or made available for issuance.

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.

Yes, the Committee believes the proposed amendments which continue to support providing decision-useful information and the benefits outweigh the costs. Derivative accounting and valuation are complex and expanding the scope exceptions to remove instruments that should be accounted for under other guidance reduces recurring costs and operational burden on companies. However, please see our response to Question 2 related to a potential requirement to apply the retrospective interest method to contracts with entity-specific underlyings that qualify for the derivative scope exception. Such a requirement could negate the potential benefits of excluding these contracts from derivative accounting, as entities may continue to avoid executing them if another complex accounting model is required to be applied.

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?

Yes, the Committee agrees that a share-based payment from a customer that is consideration for the transfer of good or services should continue to be accounted for as noncash consideration under Topic 606. As noted in paragraph 38 of the Basis for Conclusions to ASU 2016-12, the FASB concluded that the measurement date of the transaction price should not vary based on the nature of the promised consideration and indicated that measuring noncash consideration at contract inception is consistent with other aspects of the model for determining the transaction price and allocating the transaction price to performance obligations.

However, paragraph ASC 606-10-15-3A requires the accounting for the share-based payment under Topic 815 or Topic 321 when the payment from the customer is no longer contingent on the satisfaction of a performance obligation. Under Topic 606, companies also consider whether the consideration under a contract is 'variable' when determining the timing and amount of revenue to be recognized. Therefore, recognizing an asset when the performance obligation is satisfied under Topic 815 or Topic 321 could result in prematurely recognizing an asset if the uncertainty associated with the variable consideration has not been resolved. The Committee suggests the following revisions 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, 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 and, if applicable, when uncertainty associated with any variability in the amount of consideration is resolved. 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.

This proposed edit would clarify the interaction between the guidance in ASC 606-10-32 when recognizing and measuring variable consideration and the accounting for non-cash consideration as an Asset under Topic 815 and 321.

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?

The Committee is supportive of amending Topic 815 and Topic 321 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.

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

The Committee believes the requirements are operational and provide adequate and sufficient information to the preparers of the financial statements.

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.

The guidance on share-based payments received from vendors could benefit from further clarification in the proposed ASU. Practitioners currently follow ASC 705 for accounting considerations received from vendors. However, there is diversity in the accounting treatment for share-based considerations received from vendors regarding the timing and amount for recognizing the associated assets and vendor expense deductions, as the guidance in ASC 705 is not clearly prescribed. For example, some vendors provide warrants as a rebate based on the volume of purchases or goods consumed over time. We believe this diversity would be reduced if the FASB required consistent conditions for the accounting treatment of share-based consideration received from vendors.

We do not see a conceptual difference in prescribing the same accounting treatment for share-based payments received from vendors based on the proposed guidance in ASC 606. If the same accounting model were leveraged, the main accounting difference would be an increase in the revenue line item when the consideration is recognized from a customer, compared to a decrease in the vendor expense line when the consideration is recognized from a vendor. We believe this change would promote consistency in the accounting treatment for share-based consideration received from a counterparty, regardless of whether the counterparty is a customer or vendor."

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.

The Committee agrees with the transition requirement that gives entities the ability to elect to apply the proposed amendments using either a prospective approach or a retrospective approach.

Question 13: In evaluating the effective date, how much time would be needed to implement the proposed amendments? Should the effective date for entities other than public business entities be different from the effective date for public business entities? Please explain why or why not.

In evaluation of the effective date, the Committee believes that the proposed amendments should be effective for annual and interim periods beginning one year after the publication of the ASU, and no distinction should be made between public business entities and entities other than public business entities. In addition, we believe that early adoption should be permitted in any interim or annual periods in which financial statements have not yet been issued or made available for issuance.



Question 14: 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.

Yes, there should be minimal costs incurred to adopt the changes, and as discussed under Question 9, further clarity around the scoping of noncash consideration will help financial statement preparers.

Closing

We hope you find the Committee's comments and responses to the Proposed ASU informative and useful. Should you have any questions or desire further clarification on any of the matters discussed in this letter, please do not hesitate to contact the undersigned.

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