Deloitte.

April 2016

TRG Snapshot
Meeting on Revenue

by Chris Chiriatti, Joe DiLeo, Vesna Ciringer, Margaret Furry, and Denise Lucas, Deloitte & Touche LLP

In This Issue

- Topic 1 — Scope Considerations for Incentive-Based Capital Allocations, Such as Carried Interests
- Topic 2 — Considering the Class of Customer in the Evaluation of Whether a Customer Option Gives Rise to a Material Right
- Topic 3 — Scope Considerations for Financial Institutions
- Topic 4 — Evaluating How Control Transfers Over Time
- Topic 5 — Contract Asset Treatment in Contract Modifications

This *TRG Snapshot* summarizes the April 18, 2016, meeting of the revenue transition resource group (TRG) created by the FASB and IASB.

The purpose of the TRG is not to issue guidance but instead to seek and provide feedback on potential issues related to implementation of ASC 606[1] and IFRS 15[2] (collectively, the "new revenue standard"). By analyzing and discussing potential implementation issues, the TRG helps the boards determine whether they need to take additional action, such as providing clarification or issuing other guidance. The TRG comprises financial statement preparers, auditors, and users from "a wide spectrum of industries, geographical locations and public and private organizations," and board members of the FASB and IASB attend the TRG's meetings. In addition, representatives from the SEC, PCAOB, IOSCO,[3] and AICPA are invited to observe the meetings.

> **Editor's Note:** On January 21, 2016, the IASB announced that it completed its decision-making process related to clarifying the new revenue standard and that it no longer plans to schedule TRG meetings for IFRS constituents. Therefore, TRG meetings will now be FASB-only, but members of the IASB staff may participate as observers.

At the April 18, 2016, meeting (the first FASB-only session), the TRG discussed five topics, including matters related to the scope of the new revenue standard. The TRG generally agreed with the FASB staff's analyses and views regarding Topics 3, 4, and 5 and therefore did not recommend changes to the new revenue standard. The FASB staff will continue to assess and perform additional outreach on Topics 1 and 2. Consequently, Topics 1 and 2 may be addressed at a future TRG meeting.

The TRG's next meeting is scheduled for July 25, 2016.

Topic 1 — Scope Considerations for Incentive-Based Capital Allocations, Such as Carried Interests

Background: Compensation for asset managers commonly consists of both management fees (usually a percentage of assets under management) and incentive-based fees (i.e., fees based on the extent to which a fund's performance exceeds predetermined thresholds). Often, private-equity or real estate fund managers (who may be the general partner and have a small ownership percentage in the fund) will receive incentive-based fees by way of an allocation of capital from a fund's limited partnership interests (commonly referred to as "carried interests").

Under current U.S. GAAP, EITF Topic D-96[4] prescribes the accounting for incentive-based performance fees (which many entities apply to incentive-based capital allocations, including carried interests), and

[1] For titles of *FASB Accounting Standards Codification* (ASC or the "Codification") references, see Deloitte's "Titles of Topics and Subtopics in the *FASB Accounting Standards Codification*."

[2] IFRS 15, *Revenue From Contracts With Customers*.

[3] International Organization of Securities Commissions.

[4] Emerging Issues Task Force (EITF) Topic No. D-96, "Accounting for Management Fees Based on a Formula," codified in ASC 605-20-S99-1.

identifies two acceptable methods of accounting for carried interests. Under Method 1, an entity may recognize revenue for carried interests once all services are performed and all contingencies have been resolved (generally resulting in the recognition of revenue at the end of a specified measurement period — which may be the end of the contractual period). Alternatively, under Method 2, an entity may recognize revenue throughout the contract and measures it on the basis of a contractually prescribed formula (i.e., the amount that would be due from the customer if the contract is assumed to have been terminated as of each reporting date).[5]

While Example 25 in the new revenue standard contains implementation guidance that demonstrates how to apply the variable constraint to an asset management contract, the example does not specify "whether the example applies to equity-based arrangements in which the asset manager is compensated for performance-based fees via an equity interest (that is, incentive-based capital allocations such as carried interests)."[6] Consequently, the following views have been expressed by stakeholders on whether carried interests are within the scope of the new revenue standard:

- *View A* — Carried interests are within the scope of the new revenue standard.
- *View B* — Carried interests are outside the scope of the new revenue standard.
- *View C* — An entity's accounting for carried interests may vary in accordance with the nature and substance of the arrangement.

Proponents of View A believe that carried interests are revenue transactions and analogize such interests to performance bonuses in contracts with customers in other industries (i.e., they believe that the purpose of carried interest arrangements and other similar arrangements is to compensate asset managers for their services). Accordingly, under View A, carried interests would be included in the transaction price subject to the constraint guidance on variable consideration.[7] Further, entities would be required to disclose additional information about these contracts in accordance with ASC 606-10-50.

Conversely, supporters of View B believe that "the arrangements should be accounted for as an ownership interest in accordance with other GAAP"[8] because an asset manager's investment in a limited partnership may meet the definition of financial assets or financial instruments, which are outside the scope of ASC 606. Proponents of View C believe that because these arrangements vary, entities would need to apply significant judgment in evaluating their nature and substance to determine the appropriate accounting.

The FASB staff supported View A because it believes that:

- Example 25 is evidence that the Board intended asset management service contracts, including those with incentive or performance based fees, to be within the scope of ASC 606.
- Carried interests are designed to compensate an asset manager for its services (i.e., in managing and investing in the fund).
- The Board confirmed that carried interests are more akin to services than to an ownership interest when it excluded performance-based fees from an entity's consolidation analysis (i.e., in determining whether the entity is the primary beneficiary of a variable interest entity) during its deliberations of ASU 2015-02.[9]

[5] The FASB staff notes in TRG Agenda Paper 50 that it understands that diversity in practice currently exists regarding the method entities use to account for carried interests. In addition, on the basis of outreach performed, the FASB staff noted that entities that apply Method 1 "generally expressed views that the accounting model under Topic 606 is sufficient," while those applying Method 2 believed that under ASC 606, "the economics . . . would not be faithfully represented . . . especially for long-term arrangements, because revenue recognition would be deferred significantly longer than current practice."

[6] Quoted from paragraph 12 of TRG Agenda Paper 50.

[7] ASC 606-10-32-12.

[8] Quoted from paragraph 23 of TRG Agenda Paper 50.

[9] FASB Accounting Standards Update No. 2015-02, *Amendments to the Consolidation Analysis*.

For additional information, see TRG Agenda Paper 50.

Summary: After significant discussion, the TRG did not reach general agreement on whether carried interests in asset management arrangements are within the scope of ASC 606 and thus subject to the new standard's variable constraint guidance. The Board reiterated that its intention was to include these arrangements within the scope of ASC 606 because the Board viewed these incentive-based fees as compensation for services provided (i.e., part of revenue transactions). Many TRG members also noted their belief that the substance of these arrangements is to compensate asset managers for services performed (similarly to the way such arrangements are viewed today under EITF Topic D-96).

However, some TRG members noted that if the guidance in EITF Topic D-96 is removed, carried interests (i.e., the equity ownership interest in the fund that asset managers retain) may need to be evaluated under ASC 323 rather than ASC 606. The SEC observer at the meeting acknowledged this potential outcome but also noted that the SEC staff would not object if carried interests were accounted for in accordance with ASC 606. The Board and many TRG members were concerned about reaching a conclusion that carried interests were within the scope of ASC 323 because such a conclusion could affect an entity's consolidation analysis.

A Board member noted that because no general agreement was reached, the FASB would continue to consider these issues as well as whether to propose a technical correction to clarify the Board's intended treatment regarding the scope of incentive-based fees such as carried interests.

Topic 2 — Considering the Class of Customer in the Evaluation of Whether a Customer Option Gives Rise to a Material Right

Background: The new revenue standard requires an entity to determine its contractual rights and obligations, including whether options for future goods or services give rise to performance obligations under a current contract with a customer. When an option represents a material right, the entity must allocate a portion of the current contract's transaction price to the material right.

The TRG has discussed the factors an entity should consider when determining whether a material right exists and has generally concluded that the entity should take into account past, current, and future transactions as well as both qualitative and quantitative factors (including whether the right accumulates).[10]

ASC 606-10-55-42 states, in part, that an "option gives rise to a performance obligation in the contract only if the option provides a material right to the customer that it would not receive without entering into that contract (for example, a discount that is incremental to the range of discounts typically given for those goods or services to that class of customer in that geographical area or market)."

Stakeholder views have differed regarding how the class of customer should be considered in an entity's evaluation of whether a customer option gives rise to a material right. TRG Agenda Paper 54 provides the following examples of the FASB staff's views on this topic:

[10] See Deloitte's March 2016 *TRG Snapshot* for additional information.

Example	Facts	FASB Staff Analysis and Views
Volume discounts	• Company A manufactures component parts that are interchangeable, are not customized, and have various uses to multiple customers. • Company A enters into long-term master service agreements with many of its customers to provide parts. Under the agreements, the future prices of the parts depend on past volume. • For example, Company A offers Customer B a decrease in price from $1.00 per part in year 1 to $0.90 per part in year 2 if Customer B purchases more than 100,000 parts in year 1. • Early in year 1, Customer B enters into a contract with A to purchase 8,000 parts. Customer B is required to pay $1.00 for each of those 8,000 parts. • Customer C (an existing customer) places a single order for 105,000 units at a price per part of $0.90.	Company A will need to consider all relevant facts and circumstances (including the price charged to other high-volume customers) to determine whether the price offered in year 2 represents the stand-alone selling price for the part. Said differently, Company A would need to determine whether the discount (1) is incremental to the discount that would be offered to other similar customers (such as that offered to Customer C) and (2) would be offered to a similar customer independently of any prior contract the customer had with Company A. Company A would not consider pricing offered to other customers that is contingent on prior-year volume purchases. Pricing offered to Customer B that is comparable to pricing offered to other similar customers (and is offered independently of prior contracts with Company A) may be an indication that there is no incremental discount and therefore no material right. However, pricing that is not comparable may be an indication that a material right has been given to Customer B because Customer B has prepaid for parts in year 2.
Tier status	• An airline offers a "tier status" program with Bronze, Silver, and Platinum categories that are based on historical travel volume. • Benefits are offered to each tier and increase as customers reach the next tier. • Benefits may include the ability to check bags, access the airline's airport lounge, or upgrade to business-class seating. Customers without tier status would be charged fees incremental to the ticket purchase for such benefits. • Status tiers must be achieved by the end of the year and reset each year. Customers who have a larger volume of ticket purchases earn a higher status for the remainder of the current year and all of the next year. • The airline may also offer to match the level of status achieved by customers of a competitor's airline or who are identified as high-volume customers by other means (e.g., status at a hotel chain), even if they have not previously traveled with the airline.	The airline needs to evaluate whether the ticket purchase (the contract) includes a material right by determining whether the customer's option to receive discounted goods (e.g., a free checked bag) is independent of the current contract with the customer. In other words, the airline would need to consider whether the benefits (e.g., discounts) given under a tier status program are incremental to discounts given to a similar class of customer who did not enter into a prior contract with the airline. In performing the evaluation, the company could: • Compare the price it charges a certain tier of customer for the flight and the other status benefits associated with the price charged to a similar customer who does not have a prior contract. • Consider whether it would continue to offer customers status benefits for the subsequent year even if they failed to travel enough in the current year to maintain their tier status. • Assess whether, and how frequently, it would offer status benefits to a customer who demonstrates that he or she is a frequent traveler through other means (e.g., other airlines or hotels). The airline would not consider the price charged to other customers who received status benefits through prior contracts with the airline since doing so would not help it determine whether such discounted pricing is offered independently of the current contract.

The FASB staff noted that an entity will be required to use significant judgment to determine whether a material right is provided to the entity's customers. Further, the staff noted that it "is not in a position to reach broad conclusions about these types of fact patterns because there are many variations of contracts and variations in facts and circumstances that can impact the conclusion in each fact pattern."[11] However, the staff emphasized the following:

- The relative importance placed on the considerations discussed in the examples (or other considerations) will vary on the basis of an entity's facts and circumstances.
- The objective of the guidance in ASC 606-10-55-42 and 55-43 is to determine whether a customer option to receive discounted goods is independent of an existing contract with a customer.

For additional information, see TRG Agenda Paper 54.

Summary: TRG members debated the application of concepts in the framework the staff used to analyze the examples in TRG Agenda Paper 54 but did not reach general agreement on (1) how or when to consider past transactions in determining the class of customer and (2) how the class of customer should be evaluated in the determination of the stand-alone selling price of an optional good or service.

A few TRG members maintained that discounts or status achieved through past transactions is akin to accumulating features in loyalty programs (and that such features therefore represent material rights). However, others indicated that these programs represent marketing inducements (i.e., discounts) for future transactions that should be evaluated in relation to those offered to other similar customers or potential customers (e.g., other high-volume customers or potential high-volume customers). The TRG members who viewed the programs as marketing inducements believed that considering a customer's past transactions, among other factors, is appropriate in the evaluation of whether a good or service being offered to the customer reflects the stand-alone selling price for that class of customer in accordance with ASC 606-10-55-42 (particularly for entities that have limited alternative sources of information available upon which to establish a customer's class). Further, these TRG members focused on the facts that (1) similar discounts on future transactions (like those provided in the form of benefits and other offers in status programs for no additional fees) may be given to other customers who did not make or have the same level of prior purchases with the entity and (2) such discounts may be provided at the stand-alone selling price for that class of customer (i.e., the good or service is not priced at a discount that is incremental to the range of discounts typically offered to that class of customer and therefore do not represent a material right).

Because general agreement was not reached, certain Board members recommended that the staff perform additional outreach, particularly with preparers in the travel and entertainment industries and with procurement personnel in large organizations, to understand how discounts and tier status programs are negotiated and structured. After soliciting additional input, the FASB staff will determine next steps, including whether to discuss this topic at a future TRG meeting.

Topic 3 — Scope Considerations for Financial Institutions

Background: The new revenue standard excludes transactions from its scope that are accounted for under other ASC topics, including those within the scope of ASC 405 (liabilities), ASC 460 (guarantees), ASC 815 (derivatives and hedging), and ASC 860 (transfers and servicing). The new standard also notes that entities should apply ASC 606 to contracts with a customer or portions thereof if other ASC topics do not contain guidance on separation or initial measurement. To determine which guidance applies to the fees associated with certain common financial institution transactions, stakeholders have asked

[11] Quoted from paragraphs 35 and 50 of TRG Agenda Paper 54.

the FASB to clarify whether (1) mortgage servicing rights[12] should be accounted for under ASC 606 or ASC 860, (2) deposit-related fees[13] should be accounted for under ASC 405, and (3) fees from financial guarantees[14] should be accounted for under ASC 460 or ASC 815.

Mortgage Servicing Rights

The FASB staff noted that assets and liabilities associated with mortgage servicing rights traditionally have been accounted for under ASC 860 and that such practice will not change under the new revenue standard. The staff believes that servicing arrangements that are within the scope of ASC 860 are not within the scope of ASC 606 and that ASC 860 addresses both the initial recognition and subsequent measurement of mortgage servicing assets and liabilities. In the staff's view, since the subsequent measurement of the mortgage servicing assets and liabilities depends on the cash flows associated with the mortgage servicing rights, ASC 860 should be used to account for such cash flows.[15]

Deposit-Related Fees

The FASB staff noted that entities would account for revenue from deposit-related fees in accordance with ASC 606 after they adopt the new standard. Financial institutions would continue to (1) record liabilities for customer deposits because the deposits meet the definition of a liability and (2) account for customer deposits in accordance with ASC 405. However, because ASC 405 does not contain specific guidance on how to account for deposit fees, financial institutions should apply ASC 606 for deposit-related fees (i.e., in manner similar to the application of existing SEC revenue guidance by some financial institutions to account for deposit-related fees). The FASB staff suggested that implementation concerns raised by some stakeholders could be alleviated by careful analysis of the contract terms between the financial institution and the customer. Because customers generally have the right to cancel their depository arrangement at any time, the FASB staff believes that most contracts would be short term (e.g., day to day or minute to minute). As a result, revenue recognition patterns would be similar regardless of the number of performance obligations identified, and any changes to current practice would most likely be insignificant.

Fees Related to Financial Guarantees

The FASB staff noted that fees related to financial guarantees should be accounted for in accordance with either ASC 460 or ASC 815. The basis for the staff's view is partly due to its belief that "the fee would not be received unless the guarantee was made, and the guarantee liability is typically reduced (by a credit to earnings) as the guarantor is released from the risk under the guarantee."[16] Further, the staff believes that ASC 460 or ASC 815 provides a framework that addresses both initial recognition and subsequent measurement of the guarantee. In addition, the staff cited paragraph BC61 of the Basis for Conclusions of ASU 2014-09[17] as further evidence of the Board's intent to exclude guarantees from the scope of ASC 606. The staff also noted that it may suggest technical corrections to the Board to clarify the scope for fees from financial guarantees in ASC 942-825-50-2 and ASC 310-10-60-4.

See TRG Agenda Paper 52 for additional information.

Summary: The TRG generally agreed with the staff's analysis and conclusions.

[12] After originating a loan (or selling an originated loan but retaining rights to service the loan), a financial institution may perform services that include communicating with the borrower; collecting payments for interest, principal, and other escrow amounts; and performing recordkeeping activities.

[13] Deposit-related fees are those that a financial institution charges to a customer for amounts on deposit with the financial institution. Fees may be charged to give customers access their funds and to cover other activities, including recordkeeping and reporting. In addition, fees may be transaction-based (such as fees to withdraw funds through an automated teller machine) or may not be transaction-based (such as account maintenance fees).

[14] Fees charged by a financial institution to a borrower on a loan, for example, in return for the financial institution's acting as a third-party guarantor on the borrower's debt.

[15] Paragraph 11 of TRG Agenda Paper 52 notes that some entities believe that there is a close link between ASC 860's asset and liability remeasurement requirements and the collection of servicing fees (which gives rise to mortgage servicing income).

[16] Quoted from paragraph 61 of TRG Agenda Paper 52.

[17] FASB Accounting Standards Update No. 2014-09, *Revenue From Contracts With Customers*.

Editor's Note: In discussing deposit-related fees, the FASB staff was asked whether promises such as safeguarding of funds in a depository relationship represent performance obligations. The staff reminded TRG members that the materiality of promises needs to be evaluated on a basis that is consistent with the Board's recently issued guidance in ASU 2016-10.[18]

Topic 4 — Evaluating How Control Transfers Over Time

Background: Under step 5 of the new revenue standard, an entity records revenue as it satisfies performance obligations — either at a point in time or over time. If the entity meets one of the three criteria in ASC 606-10-25-27,[19] it recognizes revenue over time by using either an output method or an input method to measure its progress toward complete satisfaction of the performance obligation.[20] While the new revenue standard does not prescribe which method to use, the entity should select an approach that faithfully depicts its performance in transferring control of goods or services promised to a customer.

Stakeholders have articulated two views on whether an entity that is performing over time can transfer control of a good or service underlying a performance obligation at discrete points in time:

- *View A* — Satisfaction of any of the requirements for recognition over time implies that control does not transfer at discrete points in time. Therefore, an entity's use of an appropriate measure of progress should not result in its recognition of a material asset (e.g., work in progress) for performance the entity has completed. Proponents of View A point to paragraphs BC125, BC128, BC130, BC131, BC135, and BC142 in the Basis for Conclusions of ASU 2014-09, which clarify that control of any asset (such as work in progress) transfers to the customer as progress is made.
- *View B* — Satisfaction of any of the criteria for recognition over time does not preclude transfer of control at discrete points in time. The use of an appropriate measure of progress could therefore result in the recognition of a material asset for performance under a contract. Proponents of View B emphasized that ASC 606-10-25-27(c) specifically "contemplates transfer of control at discrete points in time." They also noted that the term "could" in paragraph BC135 implies that in certain circumstances, the customer may not control the asset as performance occurs. In addition, proponents of View B indicated that "if control can never transfer at discrete points in time, certain methods of progress referenced in the new revenue standard [e.g., milestones[21]] rarely would be permissible."[22]

The FASB staff believes that View B is inconsistent with the new revenue standard but that View A is appropriate. The staff reiterated that paragraphs BC125, BC128, BC130, BC131, BC135, and BC142 clarify that when an entity satisfies any of the three criteria for recognizing revenue over time, the entity's performance is an asset that the customer controls. The staff also indicated that under paragraph BC135, an entity would consider whether it has a right to payment in determining whether the customer controls an asset. Therefore, in the staff's view, control cannot transfer at discrete points

[18] FASB Accounting Standards Update No. 2016-10, *Identifying Performance Obligations and Licensing*. For a summary of the ASU, see Deloitte's April 15, 2016, *Heads Up*.

[19] ASC 606-10-25-27 states: "An entity transfers control of a good or service over time and, therefore, satisfies a performance obligation and recognizes revenue over time, if one of the following criteria is met:

> a. The customer simultaneously receives and consumes the benefits provided by the entity's performance as the entity performs [cross-references omitted].
>
> b. The entity's performance creates or enhances an asset (for example, work in process) that the customer controls as the asset is created or enhanced [cross-reference omitted].
>
> c. The entity's performance does not create an asset with an alternative use to the entity . . . and the entity has an enforceable right to payment for performance completed to date [cross-reference omitted]."

[20] ASC 606-10-55-16 through 55-21.

[21] Footnote 1 in TRG Agenda Paper 53 notes that as used in the discussion, "milestones" refer to measures of progress (i.e., they correlate to an entity's performance toward complete satisfaction of a performance obligation) rather than the "milestone method" under existing U.S. GAAP.

[22] Quoted from paragraph 19 of TRG Agenda Paper 53.

in time and "an appropriate measure of progress should not result in an entity recognizing a material asset that results from the entity's performance (for example, work in process)."[23]

The FASB staff also noted that (1) View A does not prohibit an entity from recognizing revenue over time if there is a period during which the entity does not perform any activities toward satisfying its performance obligation (i.e., if there is a break in the period of performance) and (2) although Example 27 in the new revenue standard refers to milestone payments, the standard does not conclude that milestones are the appropriate measure of progress. Therefore, entities must use judgment in selecting an appropriate measure of progress.

For additional information, see TRG Agenda Paper 53.

Summary: TRG members generally agreed with the FASB staff's view that the satisfaction of any of the requirements for revenue recognition over time implies that control does not transfer to the customer at discrete points in time. Consequently, an entity should not record material work in process that is associated with a performance obligation that is satisfied over time.

Certain TRG members questioned the FASB staff's view that there could be times when an entity may recognize an immaterial asset (e.g., work in progress) under a recognition-over-time model because the entity's selected measure of progress may not perfectly match its performance. Specifically, they cited ASC 340-40-25-8, which requires an entity to recognize costs related to satisfied and partially satisfied performance obligations as expenses when they are incurred.

TRG members indicated that an asset could result from activities that are not specific to the customer contract (i.e., the creation of general inventory). They reiterated the importance of understanding the differences between costs associated with the development of an asset that transfers to a customer as it is created and costs to develop assets for general inventory (i.e., before the asset undergoes modifications that are specific to the customer). One TRG member discussed an example that involved large, complex, and customized assets. He noted that activities can be performed to assemble parts, for example, and that such costs may represent inventory (and thus an asset) because the assets are interchangeable for use in more than one customer contract.

However, provided that the entity has a present right to payment, revenue recognition would begin (and the inventory would be derecognized) when the asset no longer has an alternative use (i.e., when customization of the asset to the customer's specifications begins or the other criteria for revenue recognition over time are met). Once the criteria for recognition over time are met, control of the asset transfers to the customer as the asset is created.

Topic 5 — Contract Asset Treatment in Contract Modifications

Background: Unlike current U.S. GAAP, under which there is limited guidance on accounting for modifications of revenue contracts, the new revenue standard provides an overall framework for modification accounting.[24] For example, under the new standard, when a contract modification meets the conditions in ASC 606-10-25-13(a), the modification is accounted for prospectively as a termination of the existing contract and creation of a new one. The new revenue standard also requires entities to record contract assets[25] in certain circumstances, and these assets may still be recorded at the time of a contract modification.

[23] Quoted from paragraph 20 of TRG Agenda Paper 53.
[24] ASC 606-10-25-10 through 25-13.
[25] ASC 606-10-45-1 through 45-5.

Stakeholders have expressed two views on how to subsequently account for contract assets that exist before a contract is modified when a contract modification meets the conditions in ASC 606-10-25-13(a):

- *View A* — A terminated contract no longer exists. Accordingly, contract assets associated with the terminated contract should be written off to revenue (i.e., revenue should be reversed).
- *View B* — Existing contract assets should be carried forward to the new contract and realized as receivables[26] are recognized (i.e., revenue is not reversed, leading to prospective accounting for the effects of the contract assets).

The FASB staff illustrated the effects of each view in an example of an entity (a vendor) that enters into a contract with a customer to (1) deliver a good at the beginning of the contract period and (2) provide the customer with a monthly service for a year. The example's relevant facts include the following:

- The contract consideration is $4,200, of which the entity allocates $3,000 to the good and $1,200 to the service on the basis of each stand-alone selling price.
- The customer makes no up-front payment and owes 12 equal installments of $350.
- The entity accounts for the service as a series and does not consider whether a significant financing component exists.
- Upon transfer of the good to the customer, the entity records a contract asset for $3,000 (rather than a receivable) because payment is dependent on the entity's performance of the related monthly service.
- Each month, the entity recognizes revenue of $100 as the service is performed, and it reclassifies $250 of the contract asset to a receivable because the portion of the contract asset is no longer contingent on performance of the related service.
- At the end of nine months, the parties negotiate a change in scope and price of the contract such that a year of service is added for the price of $50 per month. Therefore, the modified remaining term is 15 months.
- At the time of the modification, the total remaining consideration promised by the customer is $1,650 (($350 × 3) + ($50 × 12)), and the consideration promised by the customer that has not yet been recognized as revenue is $900 (($100 × 3) + ($50 × 12)).
- The contract asset balance is $750 ($3,000 – ($250 × 9)) when the modification is negotiated.

Under View A, the balance of the contract asset of $750 would be written off (i.e., reversed from revenue). Because of the revenue reversal, the total remaining promised consideration of $1,650 has not been recognized as revenue and would be allocated to the remaining distinct services over the modified term of 15 months. Conversely, under View B, the entity would retain the asset (i.e., not reverse revenue) and instead would allocate only the total remaining promised consideration (not yet recognized as revenue) of $900 to the remaining distinct services over the modified term of 15 months.

The FASB staff supported View B for three reasons. First, it better reflects the objective of ASC 606-10-25-13. Second, ASC 606-10-25-13(a) "explicitly states that the starting point for the determination [of the allocation in a modification] is the transaction price in the original contract *less* what had already been recognized as revenue."[27] Third, it is consistent with paragraph BC78 of the Basis for Conclusions of ASU 2014-09, which notes that the intent of ASC 606-10-25-13(a) is to avoid adjusting revenue for performance obligations that have been satisfied (i.e., such modifications would be accounted for prospectively).

[26] See ASC 606-10-45-4 for additional information.

[27] Quoted from paragraph 14 of TRG Agenda Paper 51.

For additional information, see TRG Agenda Paper 51.

Summary: The TRG generally agreed with the FASB staff's analysis and conclusions.

Editor's Note: The FASB staff noted that it has received questions about the point in time at which a receivable should be recorded under a contract with a customer (including when contract assets would be reclassified as accounts receivable). The FASB staff agreed that some confusion may result from the wording in Example 38B of the new revenue standard, which some believe is not aligned with the guidance that identifies a receivable as a right to consideration that is unconditional other than for the passage of time. The staff noted that it would ask the Board to consider a technical correction to clarify the wording in the example.

In addition, the staff noted that it has received other questions, including inquiries about situations in which performance occurs over time and whether receivables should be recorded as performance occurs or when amounts are invoiced and due. The staff noted that there is diversity in practice today regarding how and when receivables are recorded and that such diversity is not likely to be eliminated under the new standard. However, the staff reiterated that these questions do not affect revenue recognition but rather the presentation of assets on an entity's balance sheet.

Subscriptions

If you wish to receive *TRG Snapshot* and other accounting publications issued by Deloitte's National Office, please register at www.deloitte.com/us/subscriptions.

Dbriefs for Financial Executives

We invite you to participate in *Dbriefs*, Deloitte's webcast series that delivers practical strategies you need to stay on top of important issues. Gain access to valuable ideas and critical information from webcasts in the "Financial Executives" series on the following topics:

- Business strategy and tax.
- Driving enterprise value.
- Financial reporting.
- Financial reporting for taxes.
- Governance, risk, and compliance.
- Technology.
- Transactions and business events.

Dbriefs also provides a convenient and flexible way to earn CPE credit — right at your desk. Subscribe to *Dbriefs* to receive notifications about future webcasts at www.deloitte.com/us/dbriefs.

Technical Library and US GAAP Plus

Deloitte makes available, on a subscription basis, access to its online library of accounting and financial disclosure literature. Called Technical Library: The Deloitte Accounting Research Tool, the library includes material from the FASB, EITF, AICPA, PCAOB, IASB, and SEC, in addition to Deloitte's own accounting and SEC manuals and other interpretive accounting and SEC guidance.

Updated every business day, Technical Library has an intuitive design and navigation system that, together with its powerful search features, enable users to quickly locate information anytime, from any computer. Technical Library subscribers also receive *Technically Speaking*, the weekly publication that highlights recent additions to the library. For more information, including subscription details and an online demonstration, visit www.deloitte.com/us/techlibrary.

In addition, be sure to visit US GAAP Plus, our free Web site that features accounting news, information, and publications with a U.S. GAAP focus. It contains articles on FASB activities and updates to the *FASB Accounting Standards Codification*™ as well as developments of other U.S. and international standard setters and regulators, such as the PCAOB, AICPA, SEC, IASB, and IFRS Interpretations Committee. Check it out today!