

September 9, 2024

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RE: File Reference No. 2024-ED100

We appreciate the opportunity to provide feedback on the proposed Accounting Standards Update (ASU), *Derivatives and Hedging (Topic 815) and Revenue from Contracts with Customers (Topic 606)*, dated July 23, 2024. The purpose of the proposed ASU is to address stakeholders' concerns about the application of derivative accounting to contracts with features based on the operations or activities of one of the parties to the contract, and the diversity in accounting for a share-based payment from a customer that is consideration for the transfer of goods or services.

The views expressed herein are written on behalf of the Professional Standards Committee (PSC) of the Texas Society of CPAs. The committee has been authorized by the Texas Society of CPAs' Leadership Council to submit comments on matters of interest to the membership. The views expressed in this document have not been approved by the Texas Society of CPAs' Leadership Council or Board of Directors and, therefore, should not be construed as representing the views or policy of the Texas Society of CPAs.

Regarding Issue 1, the PSC is generally supportive of the Derivatives Scope Refinement. The PSC believes refining the derivatives scope is timely given the increasing number of bonds with interest payments tied to environmental, social and governance (ESG)-linked metrics. We also believe that scoping out contracts with underlyings based on operations or activities specific to one of the parties of the contract should be beneficial to reduce the number of bifurcated derivatives. However, the PSC would like to make the following observations:

- While the proposed scope exception in paragraph 815-10-15-59(e) is understandable and likely captures the embedded features that the board is targeting, we believe that the application of the proposed guidance in paragraph 815-10-15-60 will have the unintended consequence of making the derivative assessment more costly and complex for many of the more common embedded features (such as contingent conversion features and contingent redemption features). Essentially, the proposed standard would increase the complexity for any embedded feature that contains both a financial and nonfinancial underlying by requiring a fair-value-based predominant characteristics assessment. The proposed assessment may require companies to engage valuation specialists to determine which underlying has the largest expected effect on changes in the fair value of the contract just to decide if they qualify for the scope exception. The PSC acknowledges the FASB's good intention but given the unintended consequence, we recommend that the FASB reconsider this requirement. Potential solutions may be (1) to eliminate the required predominance assessment altogether and allow a scope exception for any feature that has a substantive underlying based on operations or activities specific to one of the parties of



the contract, or (2) to leave paragraph 815-10-15-60 in its current form. The PSC does not believe that the alternative that was rejected by the board as discussed in paragraphs BC31 through BC32 (which would preclude a company from applying the scope exception if a contract has any underlying that would not qualify for the scope exception) is a viable potential solution because nearly all embedded features include a financial underlying that would not qualify for the scope exception.

- The PSC believes that the proposed transition methods are operable and reasonable. The PSC believes that implementing the proposed standard in its current form may take a significant amount of time and resources for companies that elect the cumulative-effect approach in paragraph 815-10-65-8(d), particularly if they have a large number of contracts with embedded derivatives for which they would need to apply the predominant characteristics assessment. The PSC also believes that companies that adopt this standard prospectively will find the predominant characteristics assessment to be challenging. As such, sufficient lead time should be provided for both public and private companies. Further, the PSC believes private companies should be given additional time to implement the proposed amendments given their lack of resources compared to public companies.
- Because of the issue outlined in the first bullet above, the PSC does not believe the expected benefits of the proposed amendments will justify the costs due to the expected need to increase the use of valuation specialists by both entities and their accounting firms. As a result, the PSC expects a detrimental economic impact especially for small businesses. If the FASB reconsiders the requirement of a fair-value-based predominant characteristics assessment (as we have suggested above), we believe the benefits of the remaining change would justify the costs.

Regarding Issue 2, the PSC is supportive of the Scope Clarification for a Share-Based Payment from a Customer in a Revenue Contract. We believe that this amendment will promote consistency and that the benefits will outweigh the costs. However, the PSC would like to make the following observations:

- The PSC believes that further clarification may be needed to address potential conflicting guidance. We note that paragraph 606-10-15-3A states that “the share-based payment is recognized as an asset ... 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, paragraph 606-10-32-11 may require variable consideration to be estimated and recognized before a performance obligation has been fully completed (e.g., for performance obligations recognized over time). The PSC recommends that the FASB revise the wording to clarify that a contract asset may be recognized when performance obligations are partially completed in accordance with paragraph 606-10-32-11. One potential solution would be to revise ASC 606-10-15-3A as follows:
 - 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 **and recognized as a contract asset in accordance***

~~with the variable consideration guidance in paragraph 606-10-32-11 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 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.

- The PSC also recommends that the proposed paragraph ASC 606-10-15-3A be relocated immediately before paragraph 606-10-32-21. By relocating this paragraph, it would help clarify that this guidance would also apply to contracts in the scope of ASC 610-20 (without amending ASC 610-20) because ASC 610-20-32-3 already refers to ASC 606-10-32-2 through 32-27.

We appreciate the opportunity to submit comments on the proposed ASU, *Derivatives and Hedging (Topic 815)* and *Revenue from Contracts with Customers (Topic 606)*.

Sincerely,



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