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Revenue issues***Two fundamental revenue issues***

3. Many respondents to the Exposure Draft (ED) support the Bqct fuø"ghhqtvu"vq"etgcvg" a comprehensive revenue framework that improves and converges US GAAP and IFRSs. However, many respondents question whether a single model can be applied consistently across the wide range of industries within the scope of the project. In particular, many think that construction contracts are sufficiently different to justify a separate model (or an exception from the scope of the project).
4. The Boards may be able to mitigate some of those concerns through improved implementation guidance. However, the staff thinks that the concerns arise from two fundamental issues that must be resolved:
 - (a) **Control** ô some respondents questioned whether the basis of revenue recognition should be the activities of an entity rather than the transfer of goods or services to a customer. However, most respondents support the proposed core principle of recognizing revenue only when goods are services are transferred to a customer. Nonetheless, many think the ED is not sufficiently clear to help entities consistently determine when goods or services have been transferred. In particular, they request clarification on how to evaluate control for construction contracts and service contracts.
 - (b) **Separation** ô nearly all respondents have concerns with the proposed guidance on segmenting a contract and identifying separate performance obligations. Respondents think that the proposals are unclear, impractical, and could result in information that is not useful (i.e. could create units of account that are not consistent with how management of an entity and wugtu"qh"vjg"hkpcpekcn"uvcvg o gpvu"xkgy"vjg"gpvkv {øu"dwukpguu+0

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5. The comment letters on the ED include helpful suggestions on how to resolve those two fundamental issues. On the basis of that input, the staff thinks it may be necessary to articulate the model for services separately from the model for goods. That approach may appear to create more than one model, but the staff thinks that the standard still would be a single model based on the transfer of goods and services, and the basis for conclusions would explain that thinking. However, the standard simply would be drafted in a way that is easier for preparers of financial statements to understand and apply consistently.
6. Using the input from the comment letters and other outreach, the staff plans to prepare recommendations on the two fundamental issues for the Boards to consider at their joint meeting in January 2011. Those issues need to be considered together because they are interrelated.

Other (less fundamental) issues

7. Respondents have raised various other issues with the ED that the staff thinks are less fundamental than the issues of control and separation. Moreover, those issues are less interrelated which allows greater flexibility of their sequencing and staffing. Many of those issues relate to proposals that respondents found to be impractical and not cost-beneficial.
8. The following table summarizes those issues along with preliminary staff analysis

Issue	ED Proposal	Preliminary staff analysis
Contract modifications	An entity would account for a modification together with the original contract (with a cumulative adjustment) if the prices of the modification and the contract are interdependent.	The Boards need to reconsider the issue in the light of decisions they make on separation. The issue also relates to allocating changes in the transaction price.

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Issue	ED Proposal	Preliminary staff analysis
Collectibility	Collectibility would affect how much revenue is recognized rather than whether to recognize revenue. Subsequent changes in credit risk would be recognized separately from revenue.	The Boards first need to consider whether there should be an explicit recognition hurdle for assessing collectibility (in addition to the entity considering collectibility as part of its assessment of whether a contract exists). Then, they need to consider whether the effects of collectibility should be presented as an expense (as it is today) or as revenue.

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Interaction with the Leases project

9. The Boards also need to consider a couple of issues that are linked to issues in the Leases project. Those issues include:
 - (a) Licensing and rights to use \hat{o} in the revenue ED, the Boards proposed that exclusive licenses would be accounted for similarly to a lease, with revenue recognized during the license term. The Boards need to reconsider the proposal to account for a license differently depending on whether the customer has an exclusive or a non-exclusive right.
 - (b) Contracts with a put option \hat{o} in some contracts, an asset is sold with a put option. The revenue ED suggests that it would be accounted for similarly to the sale of a product with a right of return. However, in some cases the substance of the contract might be a lease or a financing transaction. The Boards need to consider the boundary between the revenue model and the lessor model.

Definition of revenue

10. The Boards previously decided to not reconsider, as part of the revenue project,

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Cost issues

11. Responses to the ED have identified various issues and concerns with the proposed cost guidance:
 - (a) Acquisition costs ò some respondents are concerned about the apparent inconsistency of the revenue proposal with other projects. Most think that at least some costs of obtaining a contract should be recognized as an asset (e.g. sales commissions and other direct incremental costs). The Boards need to reconsider their proposal in the light of decisions made in the insurance and leases projects.
 - (b) Interaction with other cost guidance ò the revenue ED intended to fill a gap in GAAP for some costs (mainly set up costs for services contracts). Many responses have questioned how the proposed guidance interacts with other cost requirements in US GAAP and IFRSs. The Boards need to determine how best to integrate the proposed cost guidance with other requirements.
 - (c) Construction and production-type costs ò responses to the ED highlight that the withdrawal of the requirements on construction and production-type contracts has resulted in the deletion of guidance that permits the recognition of some intangible assets from the costs of fulfilling a contract (e.g. learning curve costs). Those assets result from the existing focus on the recognition of profit margins throughout the contract rather than on the recognition of revenues. The Boards need to consider carefully input received on this issue (while avoiding a general reconsideration of accounting for inventory and intangible assets) to ensure they do not unintentionally create a void in existing requirements.
12. The FASB has added a full-time staff member to further analyze these cost issues. That analysis can be performed simultaneously with the redeliberation of the revenue issues noted above.

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Timeline and strategy

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- (i) Real estate,
- (ii) Breakage and gift cards,
- (iii) Customer loyalty programs,
- (iv) Rate-regulated activities,
- (v) Telecommunication services,
- (vi) Asset management fees,
- (vii) Licenses and rights to use (software, franchisors, media and entertainment),
- (viii) Pharmaceutical and biotechnology arrangements, and
- (ix) Disclosures.

Resources

18. The project team has the following resources at present.

FASB	IASB
Kenny Bement, Project Manager	*Henry Rees, Technical Principal
*Prasadh Cadambi, Practice Fellow	Glenn Brady, Senior Technical Manager
*Liz Gagnon, Assistant Project Manager (private entity focus)	
Phil Hood, Project Manager	
Mike Breen, Practice Fellow	
*Libby Biittner, PTA	
*Stephanie Stoviak, PTA	

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20. One additional staff member has just been added at the IASB (Allison). In addition, other resources may be available early next year to work on issues such as disclosures, cross-cutting issues with other projects, or other issues that can be analyzed relatively discretely.
21. The staff thinks that with these additional resources, the project will be adequately staffed.

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Appendix A Additional detail on topics for redeliberations

Transfer	Core principle of model
	Determining when a good or service is transferred
	Measuring progress