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International
Accounting Standards
Board

INFORMATION FOR OBSERVERS

Board Meeting: **22 July 2008, London**

Project: **Revenue Recognition**

Subject: **Completing the project (Agenda paper 6A)**

INTRODUCTION AND SUMMARY OF RECOMMENDATIONS

1. This paper sets out a revised plan to issue a general revenue recognition standard by June 2011. The Boards currently plan that this general revenue recognition standard will replace IAS 18 *Revenue,* IAS 11 *Construction Contracts* as well as much of the revenue recognition literature in the US. This plan takes into account the Boards' decision in May to pursue a customer consideration measurement approach.

2. In overview, this revised plan proposes that the Boards:

   - Issue a discussion paper in October/November 2008 explaining the contract-based revenue recognition model and customer consideration measurement approach. The main aim of the paper is to solicit input on whether a single revenue recognition model based on satisfying performance obligations is appropriate for all revenue contracts.

   - Immediately begin developing a draft of the exposure draft (ie before and while the discussion paper is out for comment).

   - Set June 2011 as the deadline for issuing the general revenue recognition standard.

3. The remainder of this paper considers the approach and timetable for the main steps in this plan, ie the discussion paper (paragraphs 4–29), exposure draft (paragraphs 30–44) and final standard (paragraph 45). The last section makes some overall observations about the proposed timetable (paragraphs 46–51).

DISCUSSION PAPER

Do the Boards need to issue a discussion paper?

4. Throughout 2006 and 2007, the Boards stated that the objective of the discussion paper (DP) would be to explain and illustrate two contrasting revenue recognition models (ie a customer consideration model and a fair value model). In other words, the original purpose of the DP was to educate ourselves and our constituents, and to seek input from constituents about which of the models should serve as the basis for a new general revenue recognition standard.

5. However, over the last six months, the Boards have coalesced around a single recognition model and, in May, decided to adopt the customer consideration measurement approach. (Appendix A includes a summary of the proposed model developed to date.)

6. In the staff's view, the combination of this recognition model and measurement approach will in many cases result in a pattern of revenue recognition that is similar to current practice. There are two reasons for this. First, we think that much of the current revenue literature is implicitly based on a performance obligation satisfaction model. This is because it often specifies that revenue is recognised only when economic resources (ie goods and services) are transferred to a customer (for instance consider two general standards, SAB 104 *Revenue Recognition* and IAS 18). Secondly, much of the current revenue literature measures the asset or liability arising from a contract by reference to the transaction price.

7. In view of the Boards' recent decisions, the staff reconsidered whether the Boards need to issue a DP or whether they can move straight to developing and issuing an exposure draft (ED).

8. The staff notes that it might be argued that because the proposed model is similar to much of current practice, constituents are less likely to be interested in a general discussion about the proposed model—ie a DP—and more interested in understanding how that model is going to be articulated in a standard and would apply to specific types of contracts—ie an ED.

9. Furthermore, the majority of the detailed input from constituents is likely to arise from the ED rather than the DP. In particular, the Boards will want to know whether they have articulated clear and sufficient principles that can be applied to a wide range of examples, when supported by the appropriate amount of implementation guidance. In other words, the Board will be asking whether the proposed general standard clearly addresses enough of the issues covered by current guidance while also improving weaknesses in existing guidance.

10. However, the staff continues to think that a discussion paper is necessary for two main reasons:

- a single contract-based recognition principle will be a major change of revenue recognition principle in some cases (see paragraphs 11–17 below);
- although the customer consideration measurement approach is largely familiar, the Boards are proposing significant changes to US practice (see paragraphs 18–20 below).

Major change to recognition in some cases

11. Although much of the current revenue literature is implicitly a performance obligation satisfaction model, there are other recognition principles in existing literature. In such cases, the proposed model will result in a change in when revenue is recognised.

12. The main area in which the proposed model may differ from current practice relates to construction type contracts. For instance, in IAS 11 revenue is recognised 'in the accounting period in which the work is performed' (paragraph 26). In accordance with the Boards' proposed model, revenue on such contracts would be recognised only when a performance obligation is satisfied, which would be when the *customer* has the enforceable rights or other access to the work-in-progress (WIP). In some construction contracts the WIP transfers to the customer continuously throughout the contract so, in accordance with the proposed model, revenue would in effect also be recognised as work is performed. But since a construction contract is defined only as a contract 'specifically negotiated for the construction of an asset or a combination of assets…', the staff does not think that *all* contracts within the scope of IAS 11 result in continuous transfer of the WIP. Hence, the proposed model may result in some entities that currently apply IAS 11 being precluded from recognising revenue as 'work is performed' under the contract.

13. The same may be true in US GAAP for contracts within the scope of SOP 81-1 *Accounting for Performance of Construction-Type and Certain Production-Type Contracts*. Unlike IAS 11, however, this guidance provides a basis for why revenue is recognised continuously, namely that 'the business activity taking place supports the concept that in an economic sense performance is, in effect, a continuous sale (transfer of ownership rights) that occurs as the work progresses' (paragraph 22). This basis is similar to the notion of continuously satisfying a performance obligation through transferring economic resources to the customer and, hence, is consistent with the proposed model. Nonetheless, the staff is not sure that *all* contracts within the scope of SOP 81-1 transfer economic resources continuously to the customer.

14. In the staff's view, in construction type contracts in which economic resources are not transferring to the customer throughout the contract, but for which revenue is nonetheless recognised on a percentage-of-completion basis, the asset that determines the recognition of revenue is the *WIP* rather than the contract. In other words, the revenue recognition principle is implicitly

focused on a different asset—WIP (or production asset)—compared with the proposed model.

15. Issuing a DP would give constituents the opportunity to comment on the appropriateness of a single revenue recognition principle for all revenue contracts. It would also help the Boards better understand the types of contracts and industries that might be affected by the change to a single revenue recognition principle. In particular, the Boards would find out more about contracts that currently use percentage-of-completion accounting but which are not 'continual transfer' or 'continual delivery' contracts.

16. The staff notes that if constituents argue, and the Boards subsequently agree, that in some cases revenue should be recognised as production assets are enhanced *under contract* (rather than as the contract asset increases or contract liability decreases), the Boards could consider including as part of the general standard a revenue recognition principle that focuses on the asset being created pursuant to the contract (ie the WIP). The standard would need to explain in what circumstances an entity would be allowed to recognise revenue according to this principle instead of the recognition principle based on changes in the contract.

17. For completeness, the staff notes that in some limited cases in current practice revenue is recognised even before a contract with a customer exists. For example, existing practice in the US is to recognise revenues from commodities at the completion of the production process if certain criteria are met. The proposed model would therefore alter current practices of revenue recognition if applied to these examples. However, the Boards have already concluded that the scope of the general revenue recognition standard is revenues arising in *contractual* settings. Thus there is currently no plan to change current practice for revenue recognition outside contracts. It is important to clarify this scope decision in a discussion paper to allow constituents in these industries to consider its implications.

Changes to measurement

18. Although the Boards' proposed measurement approach is similar to current practice, it requires the use of estimated standalone prices for goods and services in multiple-element contracts if there are no observable selling prices for those goods and services. This is a significant change to some US practice, particularly EITF 00-21 *Revenue Arrangements with Multiple Deliverables* and SOP 97-2 *Software Revenue Recognition*. These require the use of vendor specific or other objective evidence of prices in order to treat goods or services as a separate unit of accounting.

19. Issuing a DP would allow the Boards to understand whether constituents think that the proposed requirement to use estimated standalone prices is workable or whether it needs to be constrained in any respect. Arguably, unlike questions about the appropriateness of the single revenue recognition model, the Boards could just solicit input on this issue on the ED. Nonetheless, the staff thinks it will be useful to receive constituent feedback as early as possible.

20. Another possible issue on which input might be useful at this stage is whether some types of performance obligations may require remeasurement other than when deemed onerous. This, however, depends on the outcome of the IASB's further discussion of this issue (and is therefore related to Agenda Paper 6B).

Planned approach

21. The staff thinks that the DP should focus on the significant changes to current practice explained above. This means that the DP should explain the contract-based revenue recognition model, explain where current practice uses other revenue recognition principles and, hence, the changes that the proposed model would entail. The DP should also explain the customer consideration measurement approach and highlight where it is different from current practice (eg in its use of estimated prices). The Boards can then solicit input from constituents, particularly on the appropriateness of a single revenue recognition principle for all contracts. We think that this is the main issue on which the Boards need input at this stage.

22. We do not think there is any point in including an explanation of the exit price measurement approach, other than to note that it was considered and rejected.

23. An outline of the revised proposed DP is in Appendix B.

24. Assuming the Boards agree with the proposed objective and outline of the DP, the staff will recraft the existing draft DP chapters and develop the additional analysis. Please note that the planned approach does not call for the staff to start from scratch. It is largely a case of refocusing the draft materials that we have already developed. In addition, with the exception of remeasurement, we do not think that the issues to be discussed in the DP require any further Board deliberation.

25. The staff also envisages that a more focused DP can be shorter than the originally planned DP. This should therefore reduce the time taken to finalise the document with the Boards.

26. The proposed timetable for the DP is as follows:

Date	**Activity**
August 2008	Drafting
September 2008	Pre-ballots to Boards
October-November 2008	Ballot and issue DP
February-March 2009	Comment period end

27. The staff proposes a four-month comment period. We have some reservations about this because constituents are likely to expect a six-month comment

period on this major project. Furthermore, the comment period coincides with a holiday period and also many company year ends.

28. However, given the importance of the ED for soliciting constituents' input, the Boards need to maximise the amount of time available *after* issuing the ED to address issues raised on that document. Having a longer comment period for the DP will clearly reduce available time later in the project.

29. The staff also notes that it will be talking to some constituents who we think will be affected by the proposed model during the comment period. Nonetheless, the Boards should note the risk that some constituents who have genuine concerns about the model may get bypassed in the DP process because of the short comment period.

Q1: Does the Board agree that a DP should be issued? If so, do you agree that the main objective is to solicit comment on the appropriateness of a single revenue recognition principle for all contracts?

Q2: Does the Board agree that a four-month comment period is appropriate?

EXPOSURE DRAFT

30. Whilst the DP is being drafted and finalised, the majority of the staff team will begin work on the ED. In other words, completing the DP and starting the development of the ED will proceed in parallel.

31. Clearly it is important that work on the ED should not pre-empt feedback on the DP. But without in anyway prejudging due process, the staff thinks it unlikely that constituents will object to a contract-based recognition principle for at least a large number of contracts (because this is often current practice) nor that they will object to the measurement approach. Thus work on developing the high-level model in the DP into standards-level guidance can begin immediately. Furthermore, one of the key issues the Board is asking in the DP is whether the proposed model can be applied to all revenue contracts. This largely relates to determining the scope of the general standard rather than the model itself. Of course, for comments received on more detailed aspects of the model, any work done in the earlier stages will be updated to reflect those comments. However, we think our earlier work will be useful regardless.

Planned approach

32. The staff proposes that the first step is to create a working draft of the ED. We acknowledge that some Board members might view this as a somewhat back-to-front approach, especially since we are missing some preliminary conclusions on some critical components of a revenue recognition model (principally relating to measuring the rights in the contract).

33. However, we think that it will be useful to determine how the basic model should be articulated at the standards level at an early stage. This is because developing a draft of the ED will identify which parts of the model need to

come back to the Board for further deliberation and should bring more focus to the ensuing discussions. It will also identify any further missing components of the model. (Note that with respect to the missing pieces, the staff has already commenced work identifying these pieces and will bring them to the Boards for consideration as soon as possible.) These missing components can also be highlighted in the DP.

34. Our other rationale for starting with drafting the ED is that we plan to consider which guidance from the existing literature is compatible with the proposed model and could usefully be carried forward into the ED or could at least be used as a starting point for guidance in the ED. In other words, because of the similarity of the proposed model to much of the existing literature, we do not think each of the remaining issues has to be addressed afresh. Accordingly, the staff has already mapped current revenue literature to the list of technical issues that need to be covered in the ED.

35. The technical issues that need to be covered in the ED are listed in Appendix C.

Developing the illustrative examples

36. The other key task to start as soon as possible is the development of the illustrative examples to accompany the general standard. We have two main reasons for front ending this work.

37. First, developing the examples will highlight where the articulation of the model for the standard needs further elaboration. For example, having reviewed the existing examples in IAS 18 and SAB 104 and considered how they would work under the proposed model, we note issues relating to determining when enforceable rights to goods transfer to customer in arrangements such as consignments and layaways. And some of the upfront fee examples are good tests of the notion of a performance obligation: is there a performance obligation for the upfront activity?

38. Secondly, the examples are also needed to act as the starting point for field visits (see below).

39. At present, the staff envisages an amount of illustrative guidance that is more wide-ranging than contained in IAS 18 but, obviously, not as wide-ranging as included across all of US revenue recognition guidance. The examples will also explain how the principles of the model are applied. The lack of explanation is a big weakness in the IAS 18 examples.

Field visits and external consultation

40. The staff thinks that there is a need for field visits in the ED phase of the project. The objective of these is to explore the implications of the proposed revenue recognition model with some of the major industries that will be affected by the proposed model. Amongst these are:

- *Software industry*. The main issues to discuss are: separating performance obligations and determining standalone selling sales prices for separate goods and services that are never sold separately.

- *Construction industry*. The main issues to discuss are: determining when resources transfer to customer (eg how does an entity determine whether it or the customer has the enforceable rights to the WIP) and the role of customer acceptance in construction contracts.

- *Telecomms*. The main issues to discuss are: identifying performance obligations (including for upfront activities), separating performance obligations and determining standalone selling prices.

41. A number of companies have already expressed interest in assisting the staff. Furthermore, we can reach out via contacts on the FASB revenue recognition resource group and through industry groups coordinated by the big accounting firms. Although field visits will consume much staff time, they are a necessary and worthwhile investment that will provide useful input into developing the ED. They will also help the Boards make scope and transition decisions towards the end of deliberations.

42. The staff will need the help of one other group—a group that can advise on the development of the ED's disclosure requirements. The group should obviously be orientated towards users, but not exclusively so. (Because of this group, the staff does not think it is necessary to obtain input on disclosure from the discussion paper.)

Proposed timetable and sequencing of issues for developing the ED

43. The following table sets out the staff's proposed timetable for developing the ED (ie it excludes the DP), showing which issues we expect to bring to the Boards for deliberation.

Month	Summary of activity
2008	
Aug-Oct	Staff develop working draft of ED Staff devise and begin development of illustrative example Staff develop papers on issues relating to measuring rights in the contract
Oct	*Discussion with Board advisers*: Input on articulation of the model at the standards level and discussion of issues arising in working draft; input on appropriateness of the set of examples. *Board discussion*:

	Measuring rights I: reflecting time value of money and credit risk; variable consideration; contingent consideration; non-cash consideration
Nov	*Board discussion*: **Measuring rights** II: revenue recognition when consideration is uncertain
Dec	*Board discussion on issues from draft ED*: Confirm guidance on **identifying and combining performance obligations** (ie multiple-element arrangements)
2009	
Jan	*Board discussion on issues from draft ED*: **Treatment of typical stand-ready obligations** arising from contracts (eg returns; guarantees; statutory warranties; promotional promises; fixed price and availability guarantees)
Feb	*Board discussion on issues from draft ED*: Confirm guidance on determining **when performance obligations are satisfied** and consideration of problematic examples **Onerous contracts** (specifying when a performance obligation is deemed onerous).
Mar	*Board discussion*: **Display issues** (should revenue be reported for performance by third parties; are there any cases in which the rights and obligations in a contract should be reported gross; reporting the effects of a remeasurement) **Disclosure requirements**
Apr	*Board discussion*: Discuss DP comment letter analysis. The main issue to consider will be whether some contracts should be out of **scope of the general standard.** In particular the Boards will need to consider the potential effect on current accounting for construction type contracts.
May	*Board discussion:* Follow up on comments on DP on measurement.
Jun	*Board discussion:* **Scope and transition** (in particular transition from the many pieces of US literature)

Jul-Aug	Finalise draft of ED for Board comment
Sep	Discussion of any sweep issues arising
Oct	Ballot and Issue ED

44. The staff proposes a six-month comment period for the ED. The staff views the ED as being a critical step. The Boards will need to know whether they have articulated clear and sufficient principles, supported by the right level of guidance and illustrative examples, that can be applied to a wide range of contracts.

Q3: Does the Board agree with the approach?

Q4: Does the Board have any comments on the approach or timetable?

FINAL STANDARD

45. Assuming the project is on track at the end of the ED phase, the staff envisages a timetable along the following lines. Clearly, the amount of redeliberation required will depend on the comments received.

Month	**Activity**
Oct 2009-Mar 2010	ED comment period
Mar 2010	Roundtable discussions (if needed)
Mar-Apr 2010	Staff analysis of comment letters
May 2010	Board discussion of comment letters
June 2010-Feb 2011	Redeliberations
Mar-May 2011	Finalise, ballot and publish standard.

TIMETABLE

46. The Boards will already have noted in the above timelines that the staff proposes that the Boards complete this project by June 2011.

47. First, we think the Boards' decision to pursue the customer consideration approach allows us to refocus and streamline the DP so it is focused on the main issues on which we need input at this stage. This should speed up the process of finalising the document with the Board. Furthermore, it means that work can start immediately on the ED, which reduces the time required between the DP and ED.

48. Secondly, the decision to pursue the customer consideration approach means that the proposed model is similar to much of the current literature. As noted, we think that this should allow the Boards to use some solutions from existing literature when developing the ED, rather than starting afresh. In addition, it should also mean that we can adopt the 'life-boat' theory. That is to say, we focus on addressing the fundamental weaknesses with the existing literature first. For other issues, the Boards may need to accept adopting solutions from the current literature, even if ideally they would like to deliberate that issue to reach an improved solution.

49. Indeed, the staff now think the Boards should be clear that June 2011 is a deadline rather than a goal for this project. We note that this project started in 2002. We do not think that it is unreasonable for constituents to expect the Boards to deliver at least some improvements in revenue accounting within nine years of the start of the project, even if those improvements do not fulfil all of the Boards' initial objectives.

50. More importantly, unless the Boards issue a new standard by June 2011, many more constituents are going to be adopting IAS 18 as they transition to IFRSs. The proposed revenue recognition model as developed to date could already be used to make worthwhile improvements to IAS 18 by addressing some of its fundamental weaknesses and internal inconsistencies.

51. Clearly as with other MOU projects, the June 2011 deadline will impose a tight project timetable. Nonetheless, it will force the staff and Boards to focus on the fundamental weaknesses with current revenue recognition guidance. It also requires the staff and Boards to drive on with the decisions already reached and not go over old ground. For instance, we note that some IASB members (and staff) are attracted to a measurement approach in which the transaction price *less* some direct contract origination costs is allocated to the performance obligations. However in the staff's view, the consequences of recognising 'day 1 losses' under the customer consideration approach have been fully illustrated to the Boards and, in this project, not thought to be troubling to the majority of Board members. Hence, we do not think this issue should be redebated until the Boards have received input from constituents.

Q5: Does the Board agree that June 2011 is the deadline for completing the project?

Appendix A

SUMMARY OF BOARD DECISIONS TO DATE

A1. The Boards' proposed revenue recognition model can be summarised as follows:

a. The model addresses the recognition of contractual revenues, ie the revenues that arise when recognised contract assets increase or contract liabilities decrease (ie the net position in a contract increases).

b. At inception, a contract consists of rights and performance obligations. The rights are measured at the value[1] of promised consideration. This amount is allocated to the individual performance obligations in the contract based on the entity's observed or estimated selling prices of the goods or services underlying those performance obligations at contract inception.

c. In principle, any good or service that is promised to the customer in accordance with the explicit or implicit terms of the contract constitutes a performance obligation. In practice, for the purpose of allocating the value of the promised consideration, goods or services need to be treated as individual performance obligations only if they are transferred to the customer at different times.

d. As the entity satisfies each performance obligation in the contract, the entity recognises the corresponding increase in the contract asset or decrease in the contract liability (ie increase in the contract's net position) as revenue. The amount of revenue recognised is the amount of the consideration allocated to the satisfied performance obligation at contract inception.

e. The initial measurement of a performance obligation is locked in at inception and is not subsequently updated unless it is deemed onerous, at which point it is remeasured.[2] The IASB has indicated that there may be other circumstances in which performance obligations might be remeasured.

A2. These decisions mean that:

a. An entity recognises revenue only when a performance obligation is satisfied, ie when it transfer economic resources (ie goods and

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[1] By using the word 'value', the staff is acknowledging the possibility that the Boards may conclude that the nominal amount of the consideration should be discounted for the time value of money and the customer's credit risk. The Boards have not yet discussed this nor how the effects of any discounting should be reported in profit or loss over the contract life. The staff assumes that the unwinding of the discounting would be recognised as financing or interest revenue.

[2] The Boards have not confirmed when a contract is onerous, nor have the Boards discussed the unit of account for determining when a contract is onerous. The staff's working assumption is that a contract is onerous when an individual performance obligation is onerous. That is to say, the performance obligation itself is the unit of account for any onerous test.

services) to the customer under the contract. Revenue is not recognised when a contract is obtained, although it may be recognised immediately after contract inception if a performance obligation is satisfied.

b. At contract inception, neither a contract asset nor liability is recognised (except in the unusual circumstances that performance obligations are deemed onerous at contract inception). A contract asset or liability is recognised only when one party begins to perform in accordance with the contract (ie when the entity satisfies a performance obligation or the customer pays).

c. The total amount of revenue recognised over the life of a contract is the amount of the customer consideration.

d. The measurement approach of the proposed model differs from the prospective measurement approaches in the IASB's insurance model discussed in the 2007 paper *Preliminary Views on Insurance Contracts*. The insurance and revenue recognition project teams need to consider the interaction of the two projects.

Appendix B

PROPOSED STRUCTURE OF THE DISCUSSION PAPER

I. Project objective and purpose for discussion paper

II. Revenue and a focus on assets and liabilities

- Perceived problems with existing literature
- Explanation of focus on assets and liabilities

III. Proposed contract-based revenue recognition principle

- Rationale for proposing a single contract-based revenue recognition principle
- Contractual rights and obligations
- Changes in contractual rights and obligations

IV. Proposed measurement approach

- Measurement of performance obligations in the customer consideration approach
- Invitation to comment on the use of estimated standalone selling prices
- [Invitation to comment on whether there are types of performance obligations that call for remeasurement other than when deemed onerous]

V. Effect of the proposed revenue recognition model on current practice

- Description of the various assets and liabilities that underlie the different revenue recognition principles today (contracts, inventory, or cash).
- Comparison to current practice in major areas
- Invitation to comment on the appropriateness of a single revenue recognition principle for all contracts

Appendix: Other issues to be addressed in the exposure draft

- Brief explanation of main issues not covered in the paper but that will be addressed in the exposure draft
  - Boundary of the contract
  - Measurement of rights (eg contingent and uncertain consideration)
  - Display
  - Disclosure

Appendix C

ISSUES STILL TO BE ADDRESSED FOR A GENERAL REVENUE RECOGNITION STANDARD

C1. This list is organised according to the headings used in most accounting standards: scope, recognition, measurement, display, disclosure, implementation guidance and illustrations, effective date, and transition guidance.

Scope

C2. The Boards have already limited the scope of the standard to the recognition of revenues arising in contracts (for example, revenues from producing commodities are not in scope). The Boards have not considered whether any industries or types of contracts would be exempted from this general standard. (At this point, it is likely that insurance, leases, and financial instruments will be excluded.) The staff thinks that this will be the main issue to discuss when considering the comments on the DP. In particular, at this stage, the staff thinks that the Boards will need to consider the potential effect on some contracts accounted for under IAS 11 and SOP 81-1.

Recognition

C3. *Contracts and enforceability.* Under the customer consideration approach, the contract is not recognised until one party to the contract performs. This approach places less stress on the issue of determining when a contract exists for accounting purposes compared with the exit price measurement approach. However the Boards still need to answer the following questions in relation to this issue:

a. Is an agreement within the scope of the proposed model if the customer can effectively back out of or unwind the agreement with little or no consequence?

b. How should renewal (or cancellation) options be treated in the recognition of a contract? For instance, how should a three-year warranty contract that allows the customer to cancel at any point be treated?

b. When and how should contracts entered into (or contemplated) at the same time be combined?

d. How should contract modifications and scope changes be accounted for?

C4. *Defining and identifying performance obligations.* Identifying performance obligations in a contract is an issue that requires further clarification. **The treatment of multiple-elements arrangements is one of the major problem**

areas in current literature that must be fixed in the new standard. The Boards will need to answer the following questions in relation to this issue:

a. What (if any) guidance would be needed to assist in identifying performance obligations?

b. What (if any) guidance would be needed to assist in combining performance obligations into single units of account?

c. Do rights of return represent performance obligations? Do other similar stand-ready obligations represent performance obligations, such as (1) performance guarantees, (2) residual value guarantees, (3) non-patent-infringement guarantees, (4) minimum revenue guarantees, (5) obligations to dispose of electronic waste on behalf of the customer, (6) promotional promises, and (7) fixed-price guarantees?

d. How does the definition of performance obligations clarify gross versus net and agency issues in the current literature? Does an entity always recognize revenue when performance obligations are satisfied, even when those performance obligations are satisfied by a third party?

C5. *Changes in a contract that lead to revenue recognition* (ie satisfaction of performance obligations). The Boards will need to answer the following question in relation to this issue:

a. What constitutes satisfaction of a performance obligation? How much (if any) guidance will be required to make the notion of control or enforceable rights operable? Will the standard rely on the notion of control to determine when a performance obligation is satisfied, and will risks and rewards of ownership be ignored when they conflict with the notion of control?

Measurement

C6. The Boards have expressed a preliminary view in favor of a customer consideration measurement approach. In other words, most Board members think performance obligations should be measured at inception at a proportion of the transaction price and it is the transaction price that should be reported as revenue over the life of the contract. Nonetheless the May discussions highlighted divergent views about the extent to which performance obligations would need to be remeasured to reflect changes other than the entity's performance. For instance, the majority of FASB members indicated that performance obligations would need to be measured *only* if deemed onerous. However, the majority of IASB members indicated that remeasurement would be required beyond just onerous contract cases. In addition, the Boards have not considered issues relating to measuring the rights in the contract. The treatment of contingent and uncertain consideration is a problematic area in current literature.

C7. Hence, the Boards need to answer the following questions in relation to measurement:

Rights

a. How are rights measured? Does the measurement of rights take into account the time value of money? The customer's credit risk? How is non-cash consideration measured (eg if the customer pays with a fixed asset, trade credit, right to use an intangible asset, or even the right to use the customer's human resources)? How are barter transactions treated?

b. How are variable and contingent rights measured? Are variable and contingent amounts ignored until they are no longer uncertain, or is there some form of expected weighting calculation or even an exit price measure of those rights?

c. How are contract price adjustments reflected in the measurement of the contract and how do these affect recognised revenue? For example, consider (1) rebates (cash, eg based on annual credit card purchases, or product/other assets) (2) volume discounts, and (3) other sales incentives.

d. If the time value of money affects the measurement of rights and performance obligations, is interest accrued on those rights and performance obligations? How is the interest reported?

Performance obligations

e. What guidance will be required on estimating standalone selling prices when a good or service is never sold separately?

f. For (a) and (b) above, what effect does the measurement (and potential remeasurement) of the rights have on the measurement of the performance obligations (given that in the customer consideration approach to date, the measurement of the performance obligations is deemed equal to the measurement of the rights)?

g. When and how would a performance obligation be measured other than at an allocated amount? When would an allocated measure need to be updated (ie remeasured) after initial recognition (ie other than for performance)? For instance, when would a performance obligation be deemed to be onerous?[3] If some types of performance obligations are required to be remeasured other than when onerous, how would they be remeasured? Might it be appropriate to measure some performance obligations at fair value?

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[3] The staff proposes that if a contract is deemed onerous it is measured in accordance with current requirements for onerous contracts.

Display

C8. The Boards need to consider some issues related to how contracts, remeasurement of contracts, and revenue are displayed on the face of the financial statements:

a. Should contracts that are net assets be reported separately from contracts that are net liabilities on the statement of financial position?

b. Should the rights and the obligations be reported separately in the statement of financial position, with a subtotal representing the net position of the contract, or should the contract simply be reported net? Are there situations in which the rights and obligations should be reported gross (for example, when a contract would require specific performance)?

c. How should remeasurements (eg due to onerous contract situations) be displayed on the statement of comprehensive income? When the related performance obligations are finally satisfied, is the full remeasurement amount reported as revenue, or only the original amount attributed to that performance obligation?

Disclosure

C9. Inadequate disclosure is a weakness in current revenue accounting. The Boards need to deliberate this issue from scratch and the following questions:

a. What is the overall objective of disclosures relating to contracts with customers and changes in those contracts?

b. What disclosures within the framework of the proposed model would meet the need users?

c. How would a disclosure requirement be crafted that would require entities to report their goods and services in meaningful segments?

Implementation guidance and illustrations

C10. The Boards will need to craft some implementation guidance and illustrations to accompany this general standard.

Effective date and transition guidance

C11. The staff notes that transition and consequential amendments are likely to be a significant issue in the US because of the large amount of current literature.