
Project	Revenue Recognition
Topic	Re-exposure of the revenue standard

Introduction

1. In April 2011, the FASB and the IASB issued a progress report on their convergence work. In that report, the Boards stated that upon substantial completion of redeliberations they would consider whether re-exposure of the proposed revenue standard would be necessary. If re-exposure is not necessary, the Boards said they would develop a draft of the new standard which would be:
 - (a) made generally available, via the Boards' websites, for interested parties to review;
 - (b) used as the basis for outreach with parties that are most affected by the proposed new requirements; and
 - (c) subjected to a detailed drafting review with selected parties, as part of the fatal flaw review process each board is required to undertake.
2. Redeliberations on the revenue project are substantially complete. Hence, the purpose of this paper is to seek the Boards' views on whether it is necessary to re-expose the revised revenue model or to make a draft of the standard available on the Boards' websites as explained in the April 2011 progress report.
3. This paper is organized as follows:
 - (a) The Boards' procedures for re-exposure (paragraphs 4–6)

This paper has been prepared by the technical staff of the IFRS Foundation and the FASB for discussion at a public meeting of the FASB or the IASB.

The views expressed in this paper are those of the staff preparing the paper. They do not purport to represent the views of any individual members of the FASB or the IASB.

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- (b) Revisions to the Exposure Draft (paragraphs 7–8)
- (c) Feedback from constituents (paragraphs 9–12)
- (d) Staff analysis and questions for the Boards (paragraphs 13–15)

The Boards' procedures for re-exposure

4. The FASB's Reference Manual states the following about the issuance of a revised Exposure Draft:

165. It is not unusual for the Board to reach decisions during its redeliberations of an Exposure Draft that change the guidance proposed in the Exposure Draft. A substantive change to the guidance included in an Exposure Draft might indicate the need to issue a revised Exposure Draft. In that case, reexposure allows constituents the opportunity to raise issues/concerns not previously considered by the Board and ensures informed decision making by the Board.

166. A substantive change might result from a change that affects the scope of the Exposure Draft or that affects the substance (versus clarification) of the main recognition, measurement, or disclosure principles included in the Exposure Draft. A substantive change also might result if the Board decides to include guidance in (or remove guidance from) the Exposure Draft, depending on the effect of the change. A substantive change usually does not result from a change based on input provided by respondents in comment letters, including input on alternative approaches to resolve an issue on which the Board might be divided that is discussed in the Notice for Recipients (for example, the blockage factor issue addressed in the Exposure Draft preceding FAS 157).

167. At its public meetings, the Board discusses and reaches decisions on whether to issue a revised Exposure Draft or a final standard, generally at or near the end of its redeliberations of the Exposure Draft. The need to issue a revised Exposure Draft is a matter of judgment, considering varying factors.

- a. The extent to which decisions reached by the Board during its redeliberations of an Exposure Draft result in a substantive change to the guidance proposed in the Exposure Draft on which respondents commented (individually and/or in the aggregate).

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- b. Whether constituents have had sufficient opportunity to fully consider the implications of the change and communicate their views on the change (for example, through comment letters, roundtable meetings, and constituent outreach activities during redeliberations).
- c. Whether the Board would benefit in its decision making by additional input on the change, considering the extent to which such input would provide new information not previously considered by the Board during redeliberations.
- d. The time that has lapsed since issuance of the Exposure Draft and the effect of economic, regulatory, or other changes during the intervening period on the arrangements that are the subject of the Exposure Draft.

168. Generally, no single factor will indicate the need to issue a revised Exposure Draft. All factors potentially affecting the Exposure Draft should be considered in the aggregate. Accordingly, it might be useful to include in the Board memo for the meeting a side-by-side analysis of the substantive aspects of the guidance included in the Exposure Draft and the changes made to that guidance during redeliberations.

5. The IASB's Due Process Handbook states that:

46 After resolving issues arising from the exposure draft, the IASB considers whether it should expose its revised proposals for public comment, for example by publishing a second exposure draft.

47 In considering the need for re-exposure, the IASB:

- identifies substantial issues that emerged during the comment period on the exposure draft that it had not previously considered
- assesses the evidence that it has considered
- evaluates whether it has sufficiently understood the issues and actively sought the views of constituents
- considers whether the various viewpoints were aired in the exposure draft and adequately discussed and reviewed in the basis for conclusions on the exposure draft.

48 The IASB's decision on whether to publish its revised proposals for another round of comment is made in an IASB meeting. If the IASB

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decides that re-exposure is necessary, the due process to be followed is the same as for the first exposure draft.

6. The FASB and the IASB have similar procedures for determining whether it is necessary to issue a revised Exposure Draft. In accordance with both sets of procedures, the Boards must make the decision after considering various factors such as the nature of the changes from the Exposure Draft, the opportunity constituents have had to provide feedback on the revised proposals, and whether the issues raised by constituents were considered previously by the Boards.

Revisions to the Exposure Draft

7. The following table summarizes the changes to the Exposure Draft as a result of the Boards’ redeliberations in response to concerns expressed in the comment letters to the Exposure Draft:

Steps to apply model	Staff comments about changes from the Exposure Draft
Step 1: Identify the contract(s) with the customer	<ul style="list-style-type: none"> • No change to the definitions of a contract and a customer. • No change to the criteria for determining when a contract exists for the purpose of applying the revenue requirements. • Changed the proposed <i>indicators</i> on combining contracts to <i>criteria</i>. The criteria are limited to contracts that are entered into at or near the same time. Added a criterion for contracts for goods or services that are interrelated in design, technology, or function. • Eliminated the proposed requirement on contract segmentation (but moved the principle of price independence to Step 4 on allocating the transaction price. • Revised the guidance on contract modifications to reduce the instances in which an entity would account for a modification on a cumulative catch-up basis.
Step 2: Identify the separate performance obligations in the contract	<ul style="list-style-type: none"> • Retained the definition of a performance obligation subject to the deletion of the word “enforceable” (to clarify the proposals in the ED). • Clarified the proposals for identifying separate performance obligations (distinct goods or services) mainly by moving the guidance on a significant

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	<p>contract management service from the implementation guidance/basis to the separation requirements.</p>
<p>Step 3: Determine the transaction price</p>	<ul style="list-style-type: none"> • Modified the definition of the transaction price to refer to the amount to which the entity expects to be <i>entitled</i> rather than the expected amount to be <i>received</i>. • Modified the proposals on determining the transaction price as follows: <ul style="list-style-type: none"> ○ Collectibility: credit losses no longer included in the transaction price. Accounted for similarly to current practice (except for the presentation as contra revenue). ○ Time value of money: added a one year practical expedient and clarified when a financing component is significant. ○ Variable consideration: either a probability-weighted or a most likely amount is required (to simplify the proposals, which would have required a probability-weighted estimate in all cases). • No change to the guidance on consideration payable to a customer and on noncash consideration.
<p>Step 4: Allocate the transaction price</p>	<ul style="list-style-type: none"> • No change to the objective of allocating the transaction price (i.e. to reflect the amount to which the entity expects to be entitled). • Clarified that it may be appropriate for an entity to estimate a selling price using a residual technique if the price of a good or service is highly variable or uncertain. • Added guidance on when it is appropriate to ringfence discounts in a contract and changes in the transaction price. That guidance uses the ED’s principle of price independence (from contract segmentation) but has additional criteria to clarify when goods or services are priced independently (i.e. the payment terms relate to the particular good or service and the amount allocated to that good or service reasonable).
<p>Step 5: Recognize revenue when a performance obligation is satisfied</p>	<ul style="list-style-type: none"> • No change to the principle for determining transfer (i.e. control). • Added “risks and rewards of ownership” as an indicator of when control is transferred at a point in time. • Added the following criteria for determining when a performance obligation is satisfied over time: <ul style="list-style-type: none"> ○ The entity’s performance creates or enhances an asset that the customer controls as the asset is created or enhanced.

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	<ul style="list-style-type: none"> ○ The entity’s performance does not create an asset with alternative use to the entity and at least one of the following criteria is met: <ul style="list-style-type: none"> ▪ The customer receives a benefit as the entity executes each act of performance. ▪ Another entity would not need to reperform the act(s) completed to date if that other entity were to fulfil the remaining obligation to the customer. ▪ The entity has a right to payment for performance to date. ● No change to the objective of measuring progress toward completion of a performance obligation. <ul style="list-style-type: none"> ○ Clarified the discussion of alternative methods (i.e. output and input methods) ○ Added guidance on uninstalled materials ○ Added guidance on reasonable measures of progress ○ Clarified the meaning of abnormal costs. ● Changed the ED’s proposed constraint from an entity’s “reasonable estimate” of the transaction price to the entity being “reasonably assured” to be entitled to the amount of consideration recognized as revenue to date. No change to the factors to consider when making that determination other than to clarify that a sales-based royalty amount is not reasonably assured until the sale has been made.
Other issues	
Warranties	<ul style="list-style-type: none"> ● Revised the proposed guidance to require an entity to account for some warranties as a cost accrual, which is more consistent with current practice.
Licenses and rights to use	<ul style="list-style-type: none"> ● Eliminated the distinction between non-exclusive and exclusive licenses. All rights to use are transferred at a point in time (subject to the separation criteria and the requirements for determining and allocating the transaction price).
Onerous test	<ul style="list-style-type: none"> ● Modified the scope of the test to a performance obligation that an entity satisfies over a long period of time. Added guidance on which costs to include when performing the test (an entity would use the lower of the direct costs to satisfy the performance obligation and the amount the entity would have to pay to cancel the performance obligation).
Acquisition costs	<ul style="list-style-type: none"> ● Changed the proposal in the ED so that the incremental costs of obtaining the contract (e.g. sales commissions) are recognized as an asset. ● As a practical expedient, permitted the option to

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	<p>recognize acquisition costs as an expense if the contract is one year or less.</p> <ul style="list-style-type: none"> • Added disclosure requirements.
Fulfillment costs	<ul style="list-style-type: none"> • No change to the criteria for recognizing fulfillment costs as assets. • Clarified how an entity would amortize the asset recognized from fulfillment costs (i.e. the asset would be amortized in accordance with the transfer of goods or services to which the asset relates which might be provided in future contracts). • Clarified the guidance on how an entity would test the asset for impairment (i.e. revised the wording for precontract costs and specified whether a reversal of an impairment is required). • Added disclosure requirements. • Clarified the scope of the cost guidance developed as part of the revenue project.
Sale and repurchase agreements	<ul style="list-style-type: none"> • Added guidance to specify that an entity should account for a sale with a put option as a lease if the customer has significant economic incentive to exercise the option.
Disclosures	<ul style="list-style-type: none"> • No significant change to the proposals in the ED. • Limited the instances in which an entity would provide a maturity analysis of remaining performance obligations.
Breakage	<ul style="list-style-type: none"> • Added guidance on how to apply the model when the customer purchases a material right but chooses to not fully exercise that right (i.e. gift cards and breakage). That guidance is consistent with the ED's guidance in the example on customer loyalty points.

8. As shown in the table above, the changes from the Exposure Draft can be categorized into three main types of changes:
- (a) Clarification of the Boards' intentions with their proposals in the Exposure Draft (either by articulating the proposals differently or by adding guidance),
 - (b) Simplification of the proposals in the Exposure Draft,
 - (c) Revision of the proposals so that they align more closely with existing requirements or current practice.

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Feedback from constituents

9. Most comment letters did not suggest a need to re-expose the standard. However, some comment letters did. Consider the following quotes:

We believe that based on the outcome of re-deliberation by the boards, re-exposure of the proposed standard should be strongly considered to ensure sufficient and appropriate due process has been provided to those impacted by the Exposure Draft. [Comment Letter No. 970 from the AICPA]

We ask that the Boards also consider exposing the final proposals resulting from the Boards' redeliberations for a shortened comment period of a minimum of 60 days. We believe this will allow constituents sufficient time to identify unintended consequences, address remaining issues and ensure the final standard is of high quality. [Comment Letter No. 192 from Chevron Corporation]

We are aware that in addressing cumulatively the points in this letter and those raised by other constituents, significant changes may be necessary to the current drafting of the ED. In light of this, we believe that it is desirable for the Board to assess the scale of change necessary, and if appropriate to consider re-exposure. We are conscious that the Board is facing timetable pressures for this project, but in view of its significance, would prefer the Board to take the time necessary to ensure that constituents have adequate opportunity to comment on revised proposals. Undue haste may lead to unintended consequences and criticism of the Boards' due process. [Comment Letter No. 614 from ICAEW]

To the extent there are significant changes to the current exposure draft, we strongly suggest that the Boards re-expose the proposed standard for further review and comment considering the importance of revenue. [Comment Letter No. 503 from the IMA]

10. One of the Big 4 accounting firms recently published a document requesting that the Boards consider re-exposure of the standards being developed for revenue, leases, and financial instruments:

Obtaining robust constituent feedback is a critical part of developing high quality standards. The boards and their staffs have been working hard and have accomplished a lot in a short period. Substantial changes have been

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made to the original proposals. These standards will have a fundamental impact on the financial reporting of many companies. This leads us to conclude that re-exposing the standards and allowing ample time for constituents to formally comment is the best way for the boards to obtain the right level of input.

While informal feedback is good, a formal process is more likely to result in standards that meet investors' informational, and preparers' operational, needs while avoiding unintended consequences. Providing a broad range of constituents with an opportunity to "trial test" the revised proposed standards and comment on the actual words and associated amendments will better inform the boards about whether the actual words will be interpreted in the manner intended. Obtaining that input now, before the final standards are issued, will reduce potential implementation issues. The boards should also consider providing ample time for preparers and investors to respond to re-exposure drafts issued in similar timeframes. [PricewaterhouseCoopers' Point of View *Finding the right pace for standard setting*, May 2011]

11. In addition, the staff conducted various outreach activities during redeliberations to obtain feedback on the changes to the proposed revenue model. Feedback on the need to re-expose the proposals was mixed. Some constituents think that the number of changes to the Exposure Draft requires re-exposure for reasons similar to the reasons quoted above.
12. Other constituents think that re-exposure is not necessary, but only if a draft of the requirements is available to the public and subject to an external review. Those constituents think that feedback on the revised model would be just as useful without incurring the additional administrative costs of writing a formal comment letter.

Staff analysis and question for the Boards

13. The following table summarizes the staff's understanding of the differences between issuing a "Staff Draft" and a revised Exposure Draft (note: the Boards have not defined a staff draft as mentioned in the April 2011 Progress Report. This table is not intended to define a staff draft generally):

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	Staff Draft	Revised Exposure Draft
Objective	To ensure that the revised requirements are understandable and that the drafting of the requirements has not created unintended consequences for specific contracts or industries.	As per Staff Draft and to ask constituents whether they agree with the revised requirements.
Content	<ul style="list-style-type: none"> • summary and introduction • standard • implementation guidance • basis for conclusions • consequential amendments (FASB only: codification amendments) 	<p>As per Staff Draft and the following:</p> <ul style="list-style-type: none"> • invitation to comment • FASB in Focus • IASB Snapshot
Expected timing of issuance	July 2011 (FASB only: codification amendments issued 4–6 weeks later)	August/September 2011 (for additional time to develop the ITC and for balloting)
Exposure period	No official comment period although the staff draft would be made available for 2–3 months	3–4 month comment period (potentially longer subject to constraints arising from year-end reporting demands)
Nature of outreach during exposure period	<p>Target industries most affected by the proposals to identify any unintended consequences from the drafting of the requirements.</p> <p>Explain to users the revised requirements and their consequences.</p>	<p>Target industries most affected by the proposals to obtain feedback on the revised requirements and to identify any unintended consequences from the drafting of the requirements.</p> <p>Seek additional input from users on the revised requirements and their consequences.</p> <p>Consider holding public roundtables.</p>

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<p>Feedback reporting process</p>	<p>The Boards would jointly consider in a public meeting any sweep issues arising from feedback (i.e. issues other than drafting improvements and clarifications within the boundaries of the Boards' previous decisions). Feedback received from specific parties would not be available to the public (other than a staff-prepared summary provided to the Boards for a public discussion).</p>	<p>The Boards would redeliberate the topics on which they invited comment and any additional comments raised in response to the revised Exposure Draft. Comment letters would be available to the public through the Boards' websites.</p>
<p>Estimated timing of final standard</p>	<p>December 2011</p>	<p>September 2012</p>

14. In the staff's view, the changes to the proposals in the Exposure Draft do not in themselves require issuance of a revised Exposure Draft because all of the changes are the result of input from constituents. In accordance with the FASB's Reference Manual, a substantive change to the Exposure Draft might indicate the need for re-exposure. However, "a substantive change usually does not result from a change based on input provided by respondents in comment letters".
15. Some constituents think it would be appropriate to issue a revised Exposure Draft that invites comment on all aspects of the revised requirements even if it delays the issuance of the standard. Those constituents think that a full re-exposure is the only way to ensure a high-quality standard because of the following factors:
- (a) the breadth of scope of the revenue project,
 - (b) the risk of unintended consequences because of the scope of the project,
 - (c) the extent of change of the wording of the proposed principles in the Exposure Draft, and
 - (d) the potential for some constituents to feel that they did not have an opportunity to formally comment on the revised draft.

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16. Both the FASB's and the IASB's procedures for re-exposure suggest that re-exposure would be needed if constituents have not had an opportunity to comment on a proposal. The core principles in the Exposure Draft have remained largely intact. The changes to the Exposure Draft mostly clarified or simplified the application of those principles (and in some cases have resulted in accounting that is more consistent with existing requirements and practices). Hence, the staff thinks that constituents have had an opportunity to comment on the core principles in the revenue model. And the staff's targeted outreach during redeliberations suggests that constituents generally are pleased with the direction of the Boards' decisions to date (although they find it difficult to comment further without seeing a draft of the final standard).
17. However, it can be argued that constituents generally have not had the opportunity to comment on the revised requirements for the following:
 - (a) Determining when a performance obligation is satisfied over time (i.e. the additional guidance in response to concerns about control and services),
 - (b) Presenting the effects of credit risk adjacent to revenue,
 - (c) Constraining the cumulative amount of revenue recognized to amounts that are reasonably assured (rather than constraining the transaction price to amounts that can be reasonably estimated), and
 - (d) Applying the onerous test to a performance obligation satisfied over a long period of time.
18. If the Boards invite additional comment on the four areas listed above, the staff thinks it could be difficult to ask questions on those specific topics without also seeking input on other significant aspects of the revised requirements (e.g. identifying separate performance obligations and allocating the transaction price).
19. Moreover, if the Boards were to ask questions on specific topics, constituents are likely to treat the re-exposure as an opportunity to reopen discussion on matters that the Boards regard as being resolved (such as the core principle of recognizing revenue on the basis of the transfer of goods or services to customers).

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Redeliberating those topics could significantly delay the issuance of the final revenue standard. And the longer the project continues, the greater the risk of a loss of momentum that could delay further the issuance of a final standard.

Questions for the Boards

Questions

Do the Boards want to:

- (a) issue a Staff Draft, or
- (b) issue a revised Exposure Draft?

If the Boards decide to issue a revised Exposure Draft, do the Boards want to invite comment on all major aspects of the revised requirements? If not, on which aspects do the Boards want to invite comment?