

STAFF PAPER

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Project	Revenue Recognition		
Paper topic	Disclosures: reconciliation of contract balances and analysis of remaining performance obligations		
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Purpose of the paper

- This paper considers potential amendments to the proposed disclosure requirements in the 2011 Exposure Draft *Revenue from Contracts with Customers* (“the 2011 ED”) that would require an entity to disclose the following information:
 - a reconciliation of contract balances (paragraph 117 of the 2011 ED); and
 - an analysis of remaining performance obligations (paragraphs 119-121 of the 2011 ED).
- This paper should be read in conjunction with the January 2013 agenda paper 7E/166E, which included a summary of the feedback received on those disclosures.

Staff recommendations

- The staff recommend that the Boards replace the reconciliation of contract balances disclosure as proposed in the 2011 ED with the following alternative disclosures:
 - a narrative explanation of the changes in contract balances, comprising the following types of information:

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- (i) the opening and closing balances for an entity's contract assets and contract liabilities (this would be disclosed as quantitative data);
 - (ii) a description of an entity's contracts and typical payment terms (already required by paragraph 118 of the 2011 ED) and an explanation of the effect that those factors typically would have on the entity's contract balances; and
 - (iii) an explanation of the significant changes in the opening and closing balances of contract assets and liabilities; and
- (b) disclosure of revenue recognised in the period that arises from the amounts allocated to performance obligations satisfied in previous periods.
4. For the remaining performance obligations disclosure, the staff recommend that the Boards clarify that:
- (a) renewals that do not represent a material option are not included in the disclosure of remaining performance obligations;
 - (b) the amount of the transaction price that is allocated to the remaining performance obligations is not subject to a revenue reversal; and
 - (c) an entity is not precluded from disclosing contracts less than 12 months in the remaining performance obligations disclosure.

Structure of the paper

5. The remainder of this paper is structured as follows:
- (a) Part A: Reconciliation of contract balances (¶6-40)
 - (i) Proposed disclosure requirements (¶6-10)
 - (ii) Feedback (¶11-16)
 - (iii) Staff analysis (¶17-35)
 - (iv) Staff recommendation (¶36-40)

- (b) Part B: Analysis of remaining performance obligations (¶41-60)
 - (i) Proposed disclosure requirements (¶41-45)
 - (ii) Feedback (¶46-49)
 - (iii) Staff analysis (¶50-59)
 - (iv) Staff recommendation (¶60)
- (c) Appendix A – Summary of proposed changes
- (d) Appendix B – Example 19 from the 2011 ED
- (e) Appendix C – Example

Part A: Reconciliation of contract balances

Proposed disclosure requirements

6. In both their 2010 and 2011 exposure drafts, the Boards proposed that an entity should disclose a reconciliation from the opening to the closing aggregate balance of contract assets and contract liabilities. The Basis for Conclusions indicates that the Boards' primary objective with this disclosure is to help users understand "the relationship between the revenue recognised in a reporting period and changes in the balances of the entity's contract assets and contract liabilities" (paragraph BC254). In particular, the reconciliation of changes in those contract balances would help to explain the link between revenue and cash flows because:
- (a) contract assets (and receivables) are recognised when the entity has a right to consideration because it has satisfied a performance obligation in advance of being paid by the customer for that performance. (The difference between a contract asset and a receivable is that, for a contract asset, an entity's right to consideration is conditioned on something other than the passage of time whereas, for a receivable, the entity's right to consideration is unconditional); and
 - (b) contract liabilities are recognised when the entity is paid by the customer in advance of the entity satisfying its performance obligation to the customer.

7. The format and scope of the reconciliation proposed in the 2010 and 2011 exposure drafts were essentially the same, with only minor differences in the reconciling line items that were specified. Paragraph 117 of the 2011 ED outlines the disclosure as follows:

An entity shall disclose in tabular format a reconciliation from the opening to the closing aggregate balance of contract assets and contract liabilities. The reconciliation shall disclose each of the following, if applicable:

- a) the amount(s) recognised in the statement of comprehensive income arising from either of the following:
 - (i) revenue from performance obligations satisfied during the reporting period; and
 - (ii) revenue from allocating changes in the transaction price to performance obligations satisfied in previous reporting periods;
- b) cash received;
- c) amounts transferred to receivables;
- d) non-cash consideration received;
- e) effects of business combinations; and
- f) any additional line items that may be needed to understand the change in the contract assets and contract liabilities.

8. The Boards also included an example of this disclosure requirement in paragraph IE17/IG75. This example is included in Appendix B.
9. In developing the 2010 exposure draft, the Boards initially considered whether the reconciliation of contract balances should be presented on a gross basis (which would separately show changes in an entity's contractual rights and performance obligation) or on a net basis (ie changes in contract assets and liabilities). The Boards' conclusion on whether to require a gross reconciliation is outlined in paragraph

BC255 of the 2011 ED, which states that, “A gross reconciliation would show the remaining contractual rights and performance obligations in separate columns with a total net amount that links to the statement of financial position. In doing so, the reconciliation would highlight the amount of new contracts obtained and the amount of unsatisfied performance obligations and, hence, indicate the amount of revenue expected to be recognised in the future as a result of contracts that already exist. The Boards acknowledged that this information would be useful to users, but decided against requiring the reconciliation on a gross basis because:

- (a) the cost of preparing and auditing the reconciliation would be high because an entity would be required to measure all unperformed contracts, including executory contracts;
- (b) there is a high level of judgement inherent in executory contracts, including determining when a contract comes into existence; and
- (c) the information provided may not be useful for many types of contracts, such as those with a short duration.”

10. Following the decision to require the reconciliation to be performed on a net basis, the Boards also considered how that reconciliation should be disclosed. The Boards decided that the reconciliation of contract balances could be presented on an aggregate basis, rather than separately, for changes in the contract asset balance and the contract liability. One of the reasons for this was because some contracts will shift between a contract asset position and a contract liability position over the contract duration, which could add complexity to separate reconciliations of each balance. The staff observe, however, that a single contract could not be both a contract asset and a contract liability at the same time and, therefore, separate reconciliations could be provided.

Feedback

11. The reconciliation of contract balances disclosure, as proposed in the 2011 ED, was criticised by many respondents, including both users and preparers.

12. In principle, many users agree that an entity should provide a reconciliation of changes in their contract balances. The following comment, which was made by a user group at an outreach event that discussed the revenue proposals, explains why users are interested in such a reconciliation:

It is essential that revenue disclosures communicate the relationship between revenue recognition patterns and cash flow collections as these are critical to enterprise valuation...disclosures on contract assets and liabilities should facilitate communication of cash conversion cycle.

13. However, the feedback received from users at the recent revenue disclosure and transition workshops and at other outreach events indicates that the proposed reconciliation has limitations that would reduce its usefulness. This is because:
- (a) receivables (ie unconditional rights to consideration) are not included in the reconciliation of contract balances;
 - (b) disclosing the changes in contract assets and contract liabilities on an aggregated basis can obscure the extent of any changes (and reasons for those changes) in the separate contract asset and contract liability balances; and
 - (c) a quantified and tabulated reconciliation of contract balances is preferred, but several users acknowledged that not all of the reconciling items would be individually used in their analysis.
14. Feedback from users also indicated that the information provided in the reconciliation will be more useful for some types of contracts than it will for other contracts. For instance, users commented that:
- (a) for contract assets, they would like to know when those amounts will be transferred to accounts receivable or recognised in cash. For contract liabilities, users indicated that they wanted more information on when those amounts will be recognised as revenue;

- (b) the reconciliation could be helpful in analysing specific businesses, such as businesses with long-term contracts or businesses with significant contract liability balances (eg software businesses). However, for entities with relatively high volumes of short-term contracts in which the timing difference between revenue recognition and cash collection is minimal, a reconciliation of changes in contract assets and contract liabilities will not provide much incremental information to a user to help them analyse the entity's cash conversion cycle;
 - (c) the information on contract assets and liabilities may be more useful for only some contracts where there is a significant timing difference between payment and performance, or only for contract assets or contract liabilities for only some parts of an entity's business (ie on a disaggregated or segment basis); and
 - (d) an entity should be required to disclose additional information on contract liabilities (ie deferred revenue), particularly in relation to when a contract liability balance will be recognised as revenue. Users noted that this information is currently provided by some software entities that have substantial contract liability balances. The aging (or maturity analysis) of contract liabilities is considered further in a subsequent section in the paper, which discusses the proposed disclosure for remaining performance obligations.
15. Other respondents, including preparers, questioned whether the proposed disclosure would meet its stated objective (as outlined in paragraph 6 above) and whether the benefits of the disclosure would justify the costs of its preparation and presentation in the notes to the financial statements. The main feedback from those respondents included:
- (a) the reconciliation would have limited usefulness because management does not use similar information to manage the business;
 - (b) the reconciliation would be difficult and costly to prepare, especially because some of the information required by the reconciling items is not

- currently tracked or used by management. Of greatest concern, preparers noted that including cash as a reconciling item would require direct cash flow information that may not be currently available because an entity's cash management is not directly tied to specific contract balances; and
- (c) the proposal that the reconciliation is tabulated with each reconciling item quantified is likely to encourage the disclosure of information that is prepared solely for compliance purposes rather than result in the disclosure of information that is sufficient to explain the extent and reasons for changes in the entity's contract assets and contract liabilities over the reporting period.
16. Notwithstanding the above concerns and criticisms with the proposed disclosure, many users and even some preparers acknowledged that some information included in the reconciliation could be useful in understanding the nature, amount, timing and uncertainty of revenue and cash flows from contracts with customers. Consequently, it is on the basis of this feedback that the staff have focused their attention towards identifying possible disclosures that communicate relevant information about changes in contract balances.

Staff analysis

17. The feedback received suggests that respondents are not disputing the relevance of disclosing information that can explain the changes (and/or reasons for those changes) in contract asset and contract liability balances, but that they are either disagreeing with or expressing limited support for the proposed form and scope of the reconciliation. Some similar concerns were expressed on the reconciliation that was proposed in the 2010 ED. In the 2011 ED, as a response to those concerns, the Boards clarified in paragraph 110 and in paragraph BC260 that the requirements in existing IFRSs and US GAAP, which state that an entity need not disclose immaterial information, would apply in determining when the reconciliation would need to be provided and how much detail would have to be provided in that reconciliation.

18. However, the staff think that, given the consistent feedback received on the proposed reconciliation in the 2010 and 2011 exposure drafts, incorporating the reconciliation as proposed into the final revenue standard (with the disclosure of the reconciliation being subject to general materiality considerations) is not a viable alternative. Consequently, this paper considers possible changes to the reconciliation disclosure that can meet the objective of providing users with information about the changes in the balances for contract assets and the contract liabilities and can do so in a more cost-effective manner.
19. Those possible changes to the disclosure would involve:
- (a) disclosing information on the changes in contract assets and contract liabilities in a narrative form (in contrast to the tabulated reconciliation proposed in the 2011 ED); and/or
 - (b) requiring that disclosure to be provided for only some types of contracts or businesses. Therefore, the disclosure may not apply to the entity's total contract asset and contract liability balances.

These alternatives are considered in the following sections.

Changing the form of the disclosure

20. The staff think that a narrative explanation of the changes in contract balances should comprise the following types of information:
- (a) the opening and closing balances for an entity's contract assets and contract liabilities—this would be disclosed as quantitative data;
 - (b) a description of an entity's contracts and typical payment terms (already required by paragraph 118 of the 2011 ED) and an explanation of the effect that those factors typically would have on the entity's contract balances—this information would be disclosed as qualitative information that would be intended to explain to users of the entity's financial statements the factors that create the timing difference between payment and performance, as well as the circumstances and likely timeframe in which that timing difference is expected to reverse; and

- (c) an explanation of the significant changes in the opening and closing balances of contract assets and liabilities—this information should be disclosed as a mix of qualitative and quantitative data, and the detail to be disclosed should be consistent with the reason and extent of the change. For instance, the explanation should be more detailed if the change is unexpected or unusual given the typical features of the entity’s contract and payment terms. In other words, the purpose of this aspect of the disclosure is similar to internal management reporting whereby significant variances between budgeted outcomes and actual outcomes are identified and explained to management. Thus, if there is a change in a contract balance that is atypical and material to that balance, then the entity should be required to explain the reason and extent of that change because it would affect a user’s assessment of the relationship between the revenue recognised in a reporting period and changes in the balances of the entity’s contract assets and contract liabilities.
21. Examples of changes in contract balances that might need to be explained (in accordance with paragraph 20(c) above) include:
- (a) changes to contract balances arising from business combinations (this is relevant because users want to distinguish between organic growth and acquired growth);
 - (b) cumulative catch-up adjustments to revenue (and the corresponding contract balance) arising from a change in the measure of progress, a change in the estimate of the transaction price or a contract modification;
 - (c) impairment of a contract asset; and
 - (d) a change in the timeframe for a right to consideration becoming unconditional (ie re-classified as a receivable) or for a performance obligation to be satisfied (ie the recognition of revenue arising from a contract liability) that has a material effect on the contract balances.
22. The examples above are possible circumstances that may result in changes in contract balances that are not usual or expected and that could materially affect a user’s

analysis. Consequently, the purpose of this suggested disclosure would be to identify those variances and explain the reason for and extent of the change. In contrast, material changes in contract balances that are expected and consistent with trends would not need to be separately identified in this disclosure. This might occur if, for example, an entity receives advance payments on new contracts and the size of the advance payment and the number of new contracts entered into during the reporting period is not materially different from prior periods. In addition, the staff note that materiality will always need to be considered by an entity, meaning that entities might not need to consider some types of contracts where it is clear that the balance of contract assets or liabilities on those contracts would be immaterial.

23. The staff also think that the form of this narrative disclosure should be different from the reconciliation proposed in the 2010 and 2011 exposure drafts in two other important respects:
- (a) first, an entity would be required to explain the changes in contract balance separately for contract assets and contract liabilities. Separate disclosure was requested by users and it should be easier for an entity to provide this information in a narrative disclosure; and
 - (b) second, the disclosure would not need to specifically link the revenue recognised in the reporting period to the changes in contract asset or contract liability in order to meet the conditions set out in paragraph 20(c) above. Although this might seem like a substantial difference from the reconciliation proposed in the 2011 ED, the staff note that understanding the changes in contract assets and contract liabilities that were attributed to the satisfaction of performance obligations during the reporting period would not be readily determinable under the proposed 2011 ED disclosure in any case. Therefore, that information is not lost under this approach.
24. To demonstrate the combination of quantitative and qualitative information that may be provided, consider the following example:

For some contracts, typically long-term construction contracts, the company bills the client prior to recognising revenue. Contract liabilities of \$12,197 and \$11,580

at December 31, 2011 and 2010, respectively, are included in the Consolidated Statement of Financial Position. The change in contract liabilities results from an increase in advance payments for a significant contract for which work will begin next year.

Contract assets of \$3,847 and \$3,666 at December 31, 2011 and 2010, respectively, are included in the Consolidated Statement of Financial Position and relate to short-term logistics services contracts. For these contracts, the entity recognises revenue prior to its unconditional right to consideration, which occurs because the customer receives and consumes the benefits of the entity's performance as the entity provides the logistics services, but the entity only becomes unconditionally entitled to the related consideration once the service is completed.

25. Some construction companies already currently disclose contracts in progress, providing opening and closing balances for both:
- (a) “due from customers for contract work” or “unbilled accounts receivable” (similar to contract assets); and
 - (b) “due to customers for contract work” or “deferred revenue” (similar to contract liabilities).
26. Some risks associated with this narrative disclosure approach are as follows:
- (a) a narrative disclosure permits greater flexibility in the nature and degree of the detail provided by the disclosure. Therefore, the usefulness of the disclosure is dependent on the entity's assessment of the existence of significant changes in the opening and closing balances of contract assets and liabilities that create variances that should be explained; and
 - (b) a narrative disclosure could become boilerplate text with only limited quantitative information to put the information into context. An entity would need to understand the objective and appropriately apply the Boards' intent with respect to qualitative disclosures.
27. However, the staff think that the disclosures outlined above will still provide users with useful information related to contract assets and contract liabilities, which will help them understand the cash conversion cycle. In addition, the staff observe that the

cost of providing this disclosure may not be significant because some entities that have significant contract balances (eg long term construction companies) already disclose some information relating to balances similar to contract assets (currently referred to as 'due from customers' or 'unbilled accounts receivable') and contract liabilities (currently referred to as 'due to customers' or 'deferred revenue')

28. The staff considered requiring separate rollforwards of contract assets and contract liabilities. However, the staff thought this would be as difficult to prepare as the reconciliation as proposed in the 2011 ED, and possibly even more difficult, because a contract could move back and forth between a contract asset position and a contract liability position. In addition, it may not result in the tabular format that was preferred by users. Furthermore, rollforwards would not provide a clear link to revenue because revenue could arise from accounts receivable or cash as well.

Changing the scope of the disclosure

29. As explained above, some users commented that the information on contract assets and contract liabilities may only be needed for some contracts, such as long-term service or construction contracts, or when there is a significant timing difference between payment and performance. Similar feedback was received on the 2010 ED. In developing the 2011 ED, the Boards considered whether to require an entity to disclose the reconciliation only if specified criteria are met, such as:
- (a) the contract meets specified attributes (eg it is a long-term contract or the entity operates in a particular industry); and
 - (b) the contract assets or contract liabilities are classified as non-current assets or liabilities in the statement of financial position.
30. The Boards rejected the idea because it would be difficult to clearly identify those types of contracts or industries for which a reconciliation would provide useful information. They noted that, even though the reconciliation would be useful for industries or entities with long-term construction or outsourcing contracts, there would also be other circumstances in which a reconciliation of contract balances would be useful. However, because the same feedback was provided subsequent to

publication of the 2011 ED, and because this type of change in scope may ease the burden of the disclosure for preparers, the staff think that this alternative should be re-considered.

31. If the Boards pursued this alternative, the staff think that the scope of the disclosure should be defined by reference to the attributes of the contracts for which users stated that an explanation of contract balances may be most useful. That would include contracts where there is a significant timing difference between payment and performance, which often occurs in long-term contracts. The staff think that defining the scope of the disclosure on the basis of attributes of a contract rather than the attributes of an entity or an industry would be a principles-based solution. This approach could require the entity to prepare separate disclosures if they have contracts with very different attributes (eg contracts in one business might be typically in a contract asset position and contracts in another business might be typically in a contract liability position). Consequently, the staff expect that the separate disclosures typically would include contracts from the same business line because presumably those contracts will have similar features and terms. Therefore, in practice, defining the scope of the disclosure in this way could produce a similar outcome to that which may result from requiring the disclosure based on specific industries or specific operating segments.
32. The staff think that, although related, the decision to limit the scope of the disclosure for only some types of contracts could be made independent of the decision about the form of the disclosure. In other words, the Boards could prescribe the disclosure for only some types of contracts in the form of:
- (a) the reconciliation proposed in the 2011 ED, which would be a quantitative disclosure that is presented in a table; or
 - (b) the disclosure proposed in this paper at paragraph 20.
33. However, the staff note that if the Boards decide to limit the scope of the disclosure (regardless of its form), the disclosure would apply only to a subset of the entity's contracts and, therefore, only a subset of the contract balances. Thus, the disclosure may not easily tie to the amount of contract assets or contract liabilities recognised in

the balance sheet. Therefore, if the Boards decide to limit the scope, the staff suggest that an entity would still need to provide the amount of the overall contract balance that relates to the contracts for which a reconciliation had not been completed. This is because a user would need to be able to clearly see the portion of the business for which an explanation of the contract assets and liabilities has been provided.

34. In contrast, the same practical difficulties would not exist if the Boards were to limit the scope of the disclosure but require the form proposed in paragraph 20 above (ie the amounts of contract assets and liabilities, with narrative disclosure). However, given the nature of the disclosure proposed in paragraph 20 of this paper, the staff think that it is not necessary to also limit the scope of the disclosure. This is because, as mentioned above, the disclosure in paragraph 20 should be easier for preparers to provide. In addition, although the scope limitation may result in separate disclosures for contracts with similar features and terms, which may be useful for users, it would also place stress on the principle for determining whether the disclosure should apply. Furthermore, the scope limitation will add unnecessary complexity that may ultimately limit the usefulness of the disclosure to users.
35. If the Boards were to require the disclosure proposed in paragraph 20 of this paper, an entity should not encounter the same degree of practical difficulties in preparing the disclosure. Consequently, there is also likely to be less stress placed on the principle for determining whether the disclosure should apply. However, given the nature of the disclosure proposed in paragraph 20 of this paper, the staff think that it is not necessary to prescribe a scope boundary for the disclosure. That is because paragraph 20(c) would require an entity to disclose sufficient information to explain any change in the contract balances that might materially affect a user's analysis of the entity's cash generation cycle. In the staff's view, that requirement would be expected to encourage an entity to separately explain the effects of changes in contract balances that occur for different reasons (eg the effect of performance bonuses in one business and the cumulative catch up adjustments that primarily affect a different business). In addition, the entity would not need to provide the overall contract balance related to the segments for which a reconciliation had not been completed in order to reconcile

the contract balance for the subset of contracts with the contract balance for the entity as a whole.

Staff recommendation

36. The staff think that in light of the feedback, the Boards should not prescribe the reconciliation in the form outlined in the 2011 ED. The staff recommend that instead of a tabulated reconciliation, information about changes in contract assets and contract liabilities could be communicated in a narrative disclosure that uses a combination of quantitative and qualitative data.
37. As fully described in paragraph 20, the staff think that a narrative explanation of the changes in contract balances should be comprised of the following types of information:
- (a) the opening and closing balances for an entity's contract assets and contract liabilities—this would be disclosed as quantitative data;
 - (b) a description of an entity's contracts and typical payment terms and an explanation of the effect that those factors typically would have on the entity's contract balances; and
 - (c) an explanation of the significant changes in the opening and closing balances of contract assets and liabilities.
38. The staff do not recommend changing the scope of the reconciliation of contract balances disclosure.

A minimum breakdown of revenue

39. The narrative disclosure recommended above will not include amounts allocated to performance obligations satisfied in previous periods. This was required to be disclosed in the reconciliation as proposed in the 2011 ED. However, the staff think this line item provides relevant and important information to users and think that the Boards should maintain disclosure of this useful line item. This is because the staff think that this disclosure of these amounts would provide information about the timing of revenue recognition relative to performance (which could relate to

constrained amounts or changes in transaction price). The staff think that the Boards could either:

- (a) require disclosure of only the amounts allocated to performance obligations satisfied in previous periods; or
 - (b) similar to Example 19 in the Illustrative Examples (provided in Appendix B), analyse revenue recognised in the period between:
 - (i) amounts allocated to performance obligations satisfied during the reporting period; and
 - (ii) amounts allocated to performance obligations satisfied in previous periods.
40. The staff recommend that the Boards require only disclosure of amounts allocated to performance obligations satisfied in previous periods because this is the information that is most useful and not found elsewhere in the financial statements. A full analysis of revenue that distinguishes between the amounts relating to performance obligations satisfied in the current reporting period and amounts relating to performance obligations satisfied in previous periods is not necessary, as this information can be derived from the total revenue on the statement of comprehensive income and the disclosure of amounts allocated to performance obligations satisfied in previous periods.

Question 1 - Reconciliation of contract balances

Do the Boards agree to replace the reconciliation of contract balances disclosure as proposed in the 2011 ED and with the following alternative disclosures:

(a) a narrative explanation of the changes in contract balances, comprised of the following types of information:

(i) the opening and closing balances for an entity's contract assets and contract liabilities (this would be disclosed as quantitative data);

(ii) a description of an entity's contracts and typical payment terms (already required by paragraph 118 of the 2011 ED) and an explanation of the effect that those factors typically would have on the entity's contract balances; and

(iii) an explanation of the significant changes in the opening and closing balances of contract assets and liabilities; and

(b) disclosure of revenue recognised in the period that arises from the amounts allocated to performance obligations satisfied in previous periods.

Part B: Analysis of remaining performance obligations***Proposed disclosure requirements and the objective***

41. In both the 2010 and 2011 exposure drafts, the Boards proposed that the disclosure of future revenue from contracts with customers should be the gross amount of performance obligations remaining from contracts with an original expected duration of more than one year. Paragraph BC 261 in the Basis for Conclusions indicates that the Boards determined that separately disclosing the remaining performance obligations would enable users to:

- (a) assess the risks associated with future revenues;
- (b) understand the timing and amount of revenue to be recognised from existing contracts;
- (c) analyse trends in the amount and timing of revenue;

- (d) obtain consistency in the reporting of “backlog”, which often is disclosed by entities in management commentary but calculated on a variety of bases; and
 - (e) understand how changes in judgements or circumstances might affect the pattern of revenue recognition.
42. The disclosure proposed in the 2010 and 2011 exposure drafts was essentially the same, however the 2011 ED:
- (a) adds a practical expedient which says that an entity need not provide the disclosure if it recognises revenue in accordance with paragraph 42 of the 2011 ED (the amount to which an entity has the right to invoice); and
 - (b) removes the requirement to present the remaining performance obligations in one-year time bands and instead permits an entity to use a mixture of quantitative and qualitative information to explain when the entity expects to recognise the remaining performance obligations as revenue.
43. Paragraphs 119-121 of the 2011 ED outline the disclosure as follows:
- For contracts with an original expected duration of more than one year, an entity shall disclose the following information as of the end of the current reporting period:
- a) the aggregate amount of the transaction price allocated to remaining performance obligations; and
 - b) an explanation of when the entity expects to recognise that amount as revenue.
- An entity may disclose the information in paragraph 119 either on a quantitative basis using the time bands that would be most appropriate for the duration of the remaining performance obligations or by using qualitative information.
- As a practical expedient, an entity need not disclose the information in paragraph 119 for a performance obligation if the entity recognises revenue in accordance with paragraph 42.

44. The staff have compiled an example of what this disclosure might look like in Appendix C.
45. The information required by the remaining performance obligations disclosure includes only the amount of the transaction price that has been allocated to unsatisfied performance obligations in contracts within the scope of the 2011 ED. These contracts, defined by paragraph 15 of the 2011 ED, are contracts that are not wholly unperformed or that are wholly unperformed but cannot be cancelled without penalty.

Feedback

46. Feedback on this disclosure was not as polarised between users and preparers as with other disclosures, particularly when the entity is engaged in long-term contracts and currently disclosed backlog.
47. Both groups acknowledged the usefulness of this disclosure; however, some requested the Boards to expand the disclosure to include contracts outside the scope of the revenue standard because many entities currently include a similar disclosure with this expanded scope in other public filings (ie in management’s discussion and analysis (“MD&A”) or in compliance with US SEC Regulation S-K Item 101(c)(viii)). That expanded disclosure is commonly referred to as backlog.
48. Users explained that they currently use “backlog” information, although some acknowledged that it is not a clearly defined term, which means that it is not a comparable number across entities. Some users also questioned the relationship between the remaining performance obligation disclosure and contract liabilities. Furthermore, those users thought that an explanation of when an entity expects to recognise contract liabilities as revenue would also be helpful.
49. Preparers explained that management uses this information, so these preparers think that it is a more relevant and helpful metric for users. Preparers indicated that including this disclosure in audited financial statements may be challenging because it would include estimates of when performance obligations may be satisfied, which in some cases may not be known. (Some users stated that they would appreciate more information, even if this consists of estimates.) Consistent with prior feedback, many

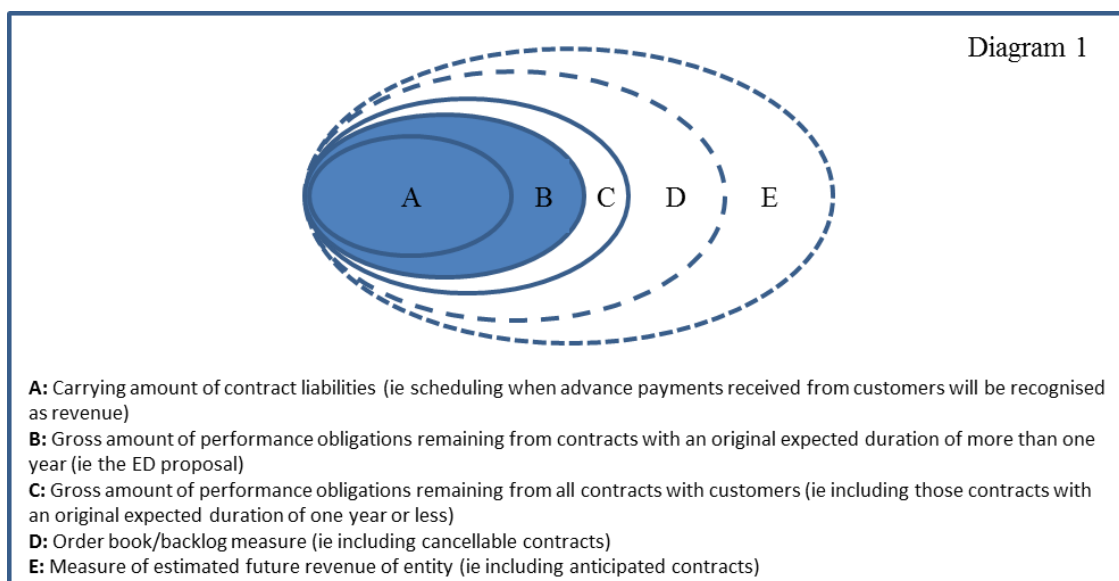
preparers, particularly those in industries that do not typically include long-term contracts, again commented that they thought the information was forward-looking and, therefore, financial statements were not the best place for this disclosure.

Staff analysis

50. Given the feedback above, in assessing whether any changes to this disclosure were necessary, the staff considered the following:
- (a) scope of the disclosure;
 - (i) interaction with backlog; and
 - (ii) interaction with contract liabilities; and
 - (b) clarifying the application of the disclosure.

Scope of the disclosure

51. The remaining performance obligation disclosure only requires disclosure of contracts within the scope of the 2011 ED (represented as C in Diagram 1 below). However, because the remaining performance obligation disclosure is most useful for longer-term contracts, paragraph 119 of the 2011 ED requires only disclosures of the remaining performance obligations for contracts with an original duration of more than one year (represented in B in Diagram 1 below).



Interaction with backlog

52. As mentioned above, some requested the disclosure of remaining performance obligations to include “backlog”. Most preparers and some users stated a preference for backlog instead of the disclosure of remaining performance obligations. Backlog is a non-GAAP number usually in the MD&A that includes remaining performance obligations under the 2011 ED, but also includes other, less firm commitments, executory contracts, projections and work that is not yet completed under “framework arrangements”. As illustrated in Diagram 1, “backlog” (D) and the remaining performance obligation disclosure (B) comprise different sets of information.
53. The Boards considered expanding the disclosure when developing the 2011 ED. However, they rejected this idea because as stated in BC264, “it would have included revenue that is outside the scope of the proposed requirements (ie the disclosure would include future contracts that are wholly unperformed and that can be terminated without penalty).”
54. The staff think this reason for rejecting the expansion in the 2011 ED is still valid. In addition, the staff think that including contracts outside the scope of the revenue ED would require the Boards to define what those contracts should be, which may be challenging. Furthermore, that scope may result in significant estimates for contracts that may be cancellable or not yet signed and, therefore, might be very costly to audit.

Interaction with contract liabilities

55. As mentioned above, some users questioned the relationship between contract liabilities and the disclosure of remaining performance obligations. Some also requested the Boards to require an entity to explain when contract liabilities will be recognised as revenue.
56. Contract liabilities represent contracts within the scope of the 2011 ED for which the entity has been paid by the customer in advance of the entity satisfying its performance obligation to the customer (represented as A in Diagram 1 above). This means that contract liabilities are a subset of remaining performance obligations. Therefore, similar to the remaining performance obligations disclosure, an explanation of when a contract liability will be satisfied could also be provided.

However, this may increase the burden of disclosure for preparers, without adding much value to users. This is because the timing of revenue recognition for both contract liabilities and other remaining performance obligations is included in the remaining performance obligation disclosure. In addition, the staff think that the narrative disclosure proposed in paragraph 20 of this paper, including the amount of contract liabilities, and the description of the entity's contracts, typical payment terms and the effect that those factors have on the entity's contract balances would be adequate for a user to understand the timing of when a contract liability will result in revenue.

Clarifying the application of the disclosure

57. A number of respondents requested the Boards clarify the application of the disclosure requirement. Many of these clarifications relate to the scope of the disclosure and what contracts and amounts should be included in the assessment of the remaining performance obligations. Specifically, some questioned whether renewal periods would be included and whether the amount of the transaction price allocated to the remaining performance obligations should include amounts that might be constrained.
58. The staff think that the Boards can clarify the scope of this disclosure in the final revenue standard. In particular, the staff think the Boards can clarify that they did not intend to require renewals that do not represent a material option to be included in the analysis of remaining performance obligations and, furthermore, that the transaction price disclosed should be the amount that would not be subject to a revenue reversal (ie the constrained amount). In addition, the staff think that the Boards can clarify that they would not preclude an entity from including contracts with durations of one year or under in this disclosure. Rather, the criterion to disclose the remaining performance obligations for contracts with an original expected duration of over one year is intended to exclude entities or contracts for which this disclosure may not be necessary.
59. Some respondents, particularly preparers, commented that this disclosure would be difficult to prepare because contracts are not distinguished by their original expected

duration. Instead, they may be tracked by their remaining durations. Some preparers said that it would be easier for them to disclose all of their contracts than to make this distinction solely for the purpose of disclosing only those contracts with an original expected duration of over one year.

Staff recommendation

60. The staff recommend that the Boards clarify the scope of the disclosure of remaining performance obligations. In particular, the staff recommend that the Boards clarify that:
- (a) renewals are not included in the disclosure of remaining performance obligations;
 - (b) the amount of transaction price that is allocated to the remaining performance obligations is not subject to a revenue reversal; and
 - (c) an entity is not precluded from disclosing contracts less than 12 months in the remaining performance obligations disclosure.

Question 2 – Analysis of remaining performance obligations disclosure

Do the Boards agree to modify the analysis of remaining performance obligations disclosure by:

- (a) renewals are not included in the disclosure of remaining performance obligations;
- (b) the amount of transaction price that is allocated to the remaining performance obligations is not subject to a revenue reversal; and
- (c) an entity is not precluded from disclosing contracts less than 12 months in the remaining performance obligations disclosure.

Appendix A

A1. The following table lists the proposed requirements from the 2011 ED that relate to the reconciliation of contract balances and analysis of remaining performance obligations disclosures, and identifies which of those proposals might change as a result of the staff recommendations in this paper.

Proposals from the 2011 Exposure Draft	Anticipated changes
<p>Reconciliation of contract balances (see paragraph IE17)</p>	
<p>117 An entity shall disclose in tabular format a reconciliation from the opening to the closing aggregate balance of contract assets and contract liabilities. The reconciliation shall disclose each of the following, if applicable:</p> <ul style="list-style-type: none"> (a) the amount(s) recognised in the statement of comprehensive income arising from either of the following: <ul style="list-style-type: none"> (i) revenue from performance obligations satisfied during the reporting period; and (ii) revenue from allocating changes in the transaction price to performance obligations satisfied in previous reporting periods; (b) cash received; (c) amounts transferred to receivables; (d) non-cash consideration received; (e) effects of business combinations; and (f) any additional line items that may be needed to understand the change in the contract assets and contract liabilities. 	<p>The staff recommend replacing the reconciliation disclosure with alternative disclosures for contract assets and contract liabilities – refer to paragraphs 36 – 40 of this paper.</p>
<p>Performance obligations</p>	
<p>118 An entity shall disclose information about its performance obligations in contracts with customers, including a description of all of the following:</p> <ul style="list-style-type: none"> (a) when the entity typically satisfies its performance obligations (for example, upon shipment, upon delivery, as services are rendered or upon completion of service); (b) the significant payment terms (for example, when payment is typically due, whether the consideration amount is variable and whether the contract has a significant financing component); 	<p>No material change is anticipated. The staff analyzed this paragraph in agenda paper 7C/167C.</p>

<p>(c) the nature of the goods or services that the entity has promised to transfer, highlighting any performance obligations to arrange for another party to transfer goods or services (ie if the entity is acting as an agent);</p> <p>(d) obligations for returns, refunds and other similar obligations; and</p> <p>(e) types of warranties and related obligations.</p>	
<p>119 For contracts with an original expected duration of more than one year, an entity shall disclose the following information as of the end of the current reporting period:</p> <p>(a) the aggregate amount of the transaction price allocated to remaining performance obligations; and</p> <p>(b) an explanation of when the entity expects to recognise that amount as revenue.</p>	<p>The staff recommend retaining the disclosure and clarifying that (a) renewals are not included in this disclosure, (b) that the amount of the transaction price that is allocated to the remaining performance obligations is not subject to a revenue reversal, and (c) that an entity would not be precluded from disclosing contracts less than 12 months – refer to paragraph 60 of this paper.</p>
<p>120 An entity may disclose the information in paragraph 119 either on a quantitative basis using the time bands that would be most appropriate for the duration of the remaining performance obligations or by using qualitative information.</p>	<p>No material change is anticipated.</p>
<p>121 As a practical expedient, an entity need not disclose the information in paragraph 119 for a performance obligation if the entity recognises revenue in accordance with paragraph 42.</p>	<p>No material change is anticipated.</p>

Appendix B – Example 19 from the 2011 ED

Reconciliation of contract assets and contract liabilities	
<p>An entity has two main business units: a services business and a retail business. Customers of the services business typically pay a portion of the promised consideration in advance of receiving the services and the remaining amount upon completion of the services. The service contracts do not include a significant financing component. Customers of the retail business typically pay in cash at the time of transfer of the promised goods.</p> <p>During 20X1, the entity recognised revenue of CU18,500 from contracts with customers (CU1,000 of which was cash sales from the entity's retail business). The entity received CU3,500 payments in advance.</p> <p>Included in the transaction price of one of the entity's services contracts is a performance bonus that the entity will receive only if it meets a specified milestone by a specified date. The entity includes that performance bonus in the transaction price and recognises revenue over time using an appropriate method of measuring progress. As of 31 December 20X0, the entity was not reasonably assured to be entitled to the cumulative amount of consideration that was allocated to the entity's past performance at that date. However, during 20X1 the entity became reasonably assured to be entitled to the performance bonus. Consequently, the entity recognised a contract asset and revenue of CU500 for the portion of the bonus relating to the entity's performance in the previous reporting period.</p> <p>As a result of a business combination on 31 December 20X1, the entity's contract assets increased by CU4,000 and its contract liabilities increased by CU1,900.</p>	
	CU
Contract assets	–
Contract liabilities	(2,000)
Net contracts at 31 December 20X0	(2,000)
Revenue from contracts with customers	
Performance obligations satisfied during the reporting period	18,000
Amounts allocated to performance obligations satisfied in previous periods	500
	<u>18,500</u>
Amounts recognised as receivables	(14,000)
Payments in advance	(3,500)
Cash sales	(1,000)
Effects of a business combination	
Increase of contract assets	4,000
Increase of contract liabilities	(1,900)
Net contracts at 31 December 20X1	100
Contract assets	<u>4,500</u>
Contract liabilities	(4,400)

IASB Agenda ref	7B
FASB Agenda ref	167B

Appendix C – Example

Illustrative Example – Option 1: Quantitative Basis

The following tables display the aggregate amount of revenue expected to be recognised in subsequent fiscal years for contracts with customers where the original expected duration exceeded one year as of contract inception.

Annual					
\$(000's)	20X3	20X4	20X5	20X6 and later	Total
Revenue expected to be recognised on contracts with customers existing as of December 31, 20X2	4,500	2,000	1,750	1,000	9,250
Quarterly					
\$(000's)	Remaining 9 months of 20X2	20X3	20X4	20X5 and later	Total
Revenue expected to be recognised on contracts with customers existing as of March 31, 20X2	6,000	4,500	2,000	2,750	15,250

Illustrative Example – Option 2: Qualitative Basis

As of December 31, 20X2, the aggregate amount of revenue expected to be recognised in subsequent fiscal years for contracts with customers where the original expected duration exceeded one year as of contract inception was \$9.25 million. Of this amount, a majority is expected to be satisfied within the next two fiscal years. The remaining amount is expected to be recognised by the end of fiscal year 20X7.