ED/2010/6
Revenue from Contracts with Customers

Kai Haussmann

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1. Background

- IASB and FASB started this project in June 2002
- IASB/FASB Discussion Paper *Preliminary Views on Revenue Recognition in contracts with Customers*
  - Published in December 2008
  - Feedback from over 220 comment letters
- ED/2010/6 *Revenue from Contracts with Customers*
  - Converged proposal with unanimous support of both the IASB and the FASB
  - Based on further development of the principles proposed in the DP using the received feedback and input from other outreach activities
  - Published for public comment on 24 June 2010
  - Comments due on 22 October 2010

2. Objective

- A single revenue recognition standard based on clear principles
  - Replace IASs 18 & 11 and most of Topic 605 in FASB Accounting Standards Codification
- Improve accounting for contracts with customers by:
  - providing a more robust framework for addressing issues as they arise
  - increasing comparability across industries and capital markets
  - providing enhanced disclosures
  - clarifying accounting for contract costs

3. Scope

- Applies to all contracts with customers except:
  - lease contracts within the scope of IAS 17 *Leases*;
  - insurance contracts within the scope of IFRS 4 *Insurance Contracts*;
  - contractual rights or obligations within the scope of IFRS 9 *Financial Instruments* or IAS 39 *Financial Instruments: Recognition and Measurement*; and
  - non-monetary exchanges between entities in the same line of business to facilitate sales to customers other than the parties to the exchange (for example, an exchange of oil to fulfil demand on a timely basis in a specified location) .

4. Core principle

Recognise revenue to depict the *transfer* of goods or services in an amount that reflects the consideration the entity receives, or expects to receive, in exchange for those goods or services.

- Revenue recognised when a good or service is transferred to a customer satisfying a performance obligation in the contract
- Amount of revenue is the amount of the transaction price allocated to the satisfied performance obligation

5. Main steps to apply the core principle

5.1 **Step 1:** Identify the contract(s) with a customer

5.2 **Step 2:** Identify the separate performance obligations in the contract

5.3 **Step 3:** Determine the transaction price

5.4 **Step 4:** Allocate the transaction price to the separate performance obligations

5.5 **Step 5:** Recognise revenue when each performance obligation is satisfied

5.1 Identify the contract(s) with a customer

Key proposal: price interdependence

- In most cases apply principle to a single contract
- Combine two or more contracts if prices are interdependent
- Segment a single contract into two or more contracts if some goods or services are priced independently of other goods and services
- Account for a modification to a contract as a part of the original contract if price is interdependent with original contract. Otherwise account for as a separate contract

5.2 Identify the separate performance obligations (1)

A performance obligation is an enforceable promise in a contract with a customer to transfer a good or service to that customer.

Key proposal: distinct goods or services

- Account for performance obligations separately if promised good or service is distinct
- A good or service is distinct if either
  - the entity, or another entity, sells an identical or similar good or service separately; or
  - the entity could sell the good or service separately because it has a distinct function and a distinct profit margin

5.2 Identify the separate performance obligations (2)

Specific implementation guidance

- Principal versus agent considerations
- Options to acquire additional goods and services (e.g. discount vouchers, customer loyalty points)
- Rights of return
- Licences and rights to use
- Product warranties and product liabilities

5.2 Identify the separate performance obligations (3)

Implementation guidance - licences

- Customer obtains control of the entire licensed intellectual property (IP) (e.g. exclusive license for economic life)
  - sale of the IP, not a licence
- Exclusive licence, but customer does not obtain control of entire licensed IP
  - performance obligation to permit customer to use IP
  - revenue is recognised over time
- Non-exclusive licence
  - performance obligation to transfer licence
  - revenue when the customer is first able to use the licence

5.2 Identify the separate performance obligations (4)

Implementation guidance - warranties

- Cover for latent defects (‘quality assurance’ warranty)
  - not a performance obligation
  - requires evaluation of whether the performance obligation to transfer the product is satisfied
  - revenue not recognised until the defective product or component of the product is replaced
- Cover for faults arising after the transfer of the product (‘insurance’ warranty)
  - is a performance obligation
  - revenue is recognised over the warranty period

5.3 Determine the transaction price

Key proposal: expected amount

- The transaction price is the expected (probability-weighted) consideration from the customer, and reflects:
  - reasonable estimates of contingent amounts (if experience of identical or similar contracts and expectation that circumstances will not change significantly)
  - the customer's credit risk
  - the time value of money (if implicit financing is included)
  - non-cash considerations measured at fair value

5.4 Allocate the transaction price

Key proposal: relative selling price allocation

- Allocate the transaction price to all separately identified performance obligations in proportion to standalone selling prices
- The standalone selling price of a good or service is the price at which the entity would sell that good or service if it was sold separately at contract inception
- Standalone selling prices have to be estimated if they are not observable
- Application of the residual method is prohibited

5.5 Recognise revenue when a performance obligation is satisfied

Key proposal: transfer based on control

- Recognise revenue when a performance obligation is satisfied by transferring a good or service to the customer
- A good or service is transferred when the customer obtains control of it
- Transfer of control can be at a point in time or can be continuous (but only, if the customer controls the work-in-progress)

A customer obtains control when the customer has the ability to direct the use of, and receive the benefit from, a good or service.

6. Onerous performance obligations

- A performance obligation is onerous if the direct costs to satisfy the obligation exceed the allocated transaction price
- Recognise a separate liability and corresponding contract loss
- Direct costs are all costs that relate directly to the contract or incurred only because of the contract

7. Proposed cost guidance

- Costs may give rise to an asset recognised in accordance with other standards (e.g. IAS 2 *Inventories*)
- If not, recognise contract fulfilment costs as a contract asset if those costs:
  - relate directly to a contract (or a specific contract under negotiation)
  - generate or enhance resources of the entity that will be used in satisfying performance obligations in the future and
  - are expected to be recovered
- Expense all costs of obtaining a contract

8. Proposed disclosure requirements

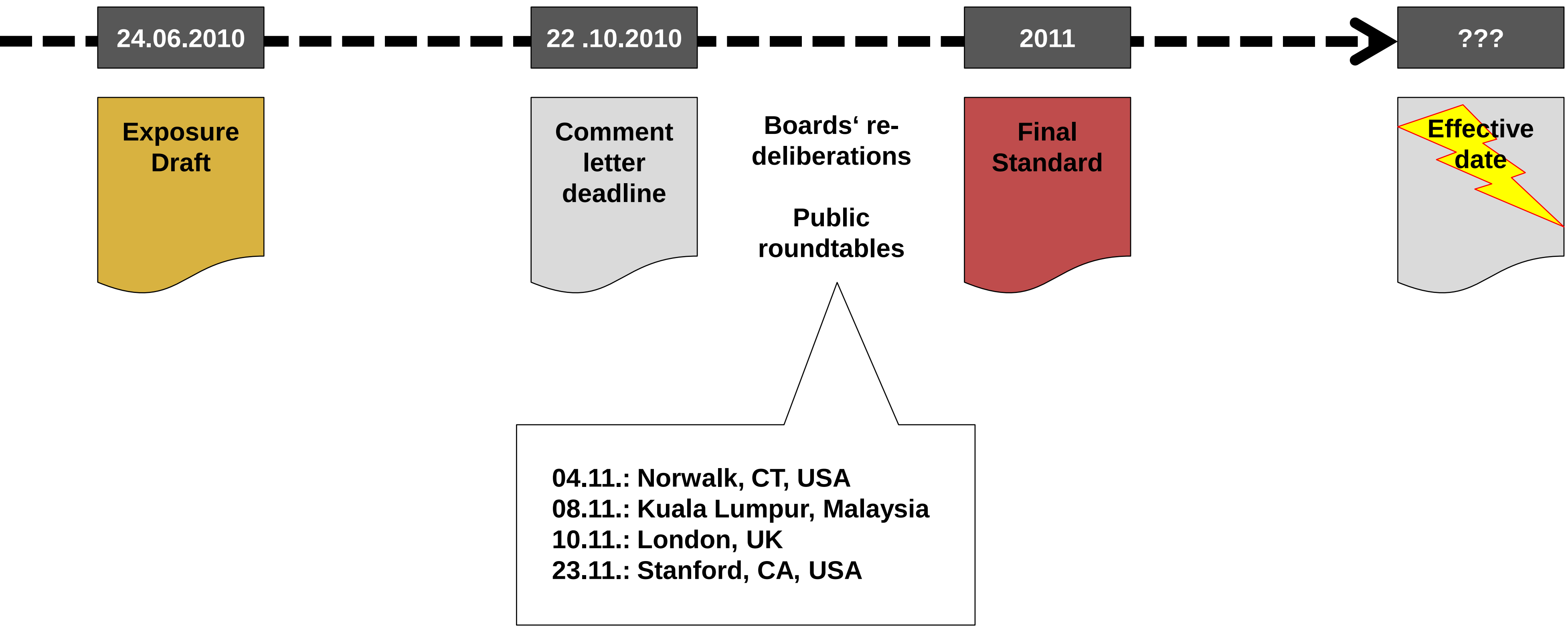
Enhanced disclosures to help users understand the amount, timing and uncertainty of revenue and cash flows

- Information about contracts with customers
  - disaggregation of revenue
  - nature of performance obligations and additional information about onerous performance obligations
  - maturity analysis of remaining performance obligations in contracts with original duration of more than one year
  - reconciliation from opening to closing total contract balances
- Information about judgments and changes in judgments
  - continuously satisfied performance obligations
  - determining and allocating the transaction price

9. Effective date and transition

- Effective date not yet determined
- Full retrospective application
- Early adoption – tentative decisions:
  - permitted for first time adopters of IFRSs
  - not yet decided whether to permit for existing IFRS preparers
- The Boards will consult publicly on transition and effective date for a range of projects

10. Next steps



Deutsches Rechnungslegungs Standards Committee e.V.
Accounting Standards Committee of Germany ®

Vielen Dank für Ihre Aufmerksamkeit!

WP/StB Kai Haussmann

DRSC e.V.
Zimmerstr. 30
10969 Berlin

Tel. 030 20 64 12 14
Fax 030 20 64 12 15

www.drsc.de
haussmann@drsc.de