

Hot Topic

Update on major accounting
and auditing activities



Revenue recognition – FASB and IASB discuss redeliberation plan

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At the 17 November 2010 meeting, the staff of the Financial Accounting Standards Board and the International Accounting Standards Board (collectively, “the staff”) provided the two Boards with a brief update on the status of the revenue recognition project.¹ The staff reviewed the issues identified thus far and their proposed timeline for bringing the issues to the Boards for redeliberation. The staff anticipates that a full comment letter analysis will be presented to the Boards in December and redeliberations will occur beginning in January.

Initial feedback received

The staff updated the Boards on their analysis of the approximately 1,000 comment letters received on the revenue recognition exposure draft. Approximately one-third of those letters were “form letters” submitted by various entities in or closely related to the construction industry, with the remainder of the letters received from a wide variety of industries. The staff indicated that their full comment letter analysis is ongoing and they expect to

present a summary of the comment letters during the December joint Board meetings.

Based on their preliminary analysis of the comment letters, as well as the feedback provided by participants in the roundtables held in Norwalk, London and Kuala Lumpur,² the staff believes that there are two fundamental aspects of the proposed revenue recognition model that will likely require further Board deliberation:

- ▶ The concept of “control” as proposed in the exposure document requires further development to clarify when control transfers in certain arrangements; particularly in long-term construction projects and in arrangements to provide services.
- ▶ The proposed guidance on the separation of promised goods and services into distinct performance obligations is not sufficient or practical for many transactions and requires further development.

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¹ Proposed Accounting Standards Update, *Revenue Recognition* (Topic 605)

² The Boards will host one additional roundtable event in Stanford, CA on 23 November 2010 as a part of the initial outreach program.

The staff also highlighted other common concerns with the guidance on:

- ▶ The use of probability-weighted estimates in the model
- ▶ Time value of money and collectibility
- ▶ Accounting for warranties
- ▶ Onerous performance obligations
- ▶ Contract costs – particularly contract acquisition costs
- ▶ Retrospective application upon transition

Finally, the staff indicated that while the Boards were commended for their efforts on the revenue project during the roundtable process, certain constituents emphasized the need for the Boards to field test the model to avoid unintended consequences.

Tentative redeliberation plan

The staff indicated that they plan to address the two fundamental issues – control and separation – at the January board meetings. During the Q&A session following the update, the staff indicated they will present for the Boards' consideration a "transfer" model that they believe will help the construction industry and entities applying the model to services arrangements. The staff anticipates bringing papers to the Boards for consideration on the other topics identified beginning in January 2011. The staff indicated that additional staff resources have been added to the project to assist in the analysis of the items identified for redeliberation.

Looking ahead

The Boards' published project plans and other public comments indicate that they intend to issue a final standard before 30 June 2011. During the discussion, the Boards did not suggest that deadline would not be met, and the allocation of additional resources to the project suggests that the Boards will make every effort to meet that deadline. We will continue to provide updates as the Boards reach significant conclusions on this project.

Resources

The following Ernst & Young documents are available to assist interested parties in understanding the proposals set forth in the revenue project:

- ▶ Hot Topic 2010-32: *FASB proposes single revenue recognition model* (SCORE No. BB1962)
- ▶ Financial Reporting Developments: *The road to convergence: the revenue recognition proposal* (SCORE No. BB1991)
- ▶ Technical Line 2010-10: *The road to convergence: the revenue recognition proposal – Telecommunications* (SCORE No. BB2015)
- ▶ Technical Line 2010-11: *The road to convergence: the revenue recognition proposal – Retail and consumer products* (SCORE No. BB2014)
- ▶ Technical Line 2010-13: *The road to convergence: the revenue recognition proposal – Oil and gas* (SCORE No. BB2018)

- ▶ Technical Line 2010-14: *The road to convergence: the revenue recognition proposal – Media and entertainment* (SCORE No. BB2026)
- ▶ Technical Line 2010-15: *The road to convergence: the revenue recognition proposal – Software* (SCORE No. BB2027)
- ▶ Technical Line 2010-16: *Any future for sell-through accounting?* (SCORE No. BB2031)

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