Power and Utilities Alert
Exposure Draft - Revenue from Contracts with Customers

Alert 2011-7
November 15, 2011

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The updated FASB/IASB exposure draft will replace substantially all of the existing revenue guidance in GAAP

Overview

On November 14, 2011, the Financial Accounting Standards Board (FASB) and the International Accounting Standards Board (IASB, or together with the FASB, the Boards) issued an updated joint exposure draft (ED) entitled *Revenue from Contracts with Customers*. The Boards' initial revenue recognition exposure draft was issued in June 2010. The new ED was issued following a lengthy period of redeliberation in response to constituent feedback on the Boards' initial proposal.

The ED will require careful consideration by power and utility reporting entities, including an evaluation of the potential impact of the proposal on the way in which revenue from power contracts is recognized. While most of the potential issues impacting the industry are consistent with those stemming from the Boards' original proposal, there has been one significant development since the original 2010 exposure draft. The FASB had previously proposed that the existing guidance in ASC 980, *Regulated Operations,* for alternative revenue arrangements and revenue subject to refund be superseded, however, as previously discussed in Power and Utilities Alert 2011-3, the FASB decided in July 2011 that it would retain the existing guidance, while adding a new requirement to separately disclose amounts recognized related to alternative revenue arrangements. The details of this new requirement (and the form in which the previous guidance for regulated entities is to be retained) will not become clear until the FASB releases the consequential amendments to the FASB Codification. These will be issued for public comment prior to March 12, 2012.

The ED has a 120-day comment period and the target date for issuing a final standard is now September 2012. The effective date is expected to be no earlier than annual periods beginning on or after January 1, 2015. The FASB will not allow for early adoption, although it is expected that the IASB will permit early adoption for IFRS preparers.

The table below summarizes some of the issues critical to the power and utility industry which may be relevant to reporting entities as they consider responding to the ED. These issues are not new but now require further focus as the potential issuance date of the new guidance moves closer. Furthermore, depending on the evolution of the Boards' separate project on leases, more power sales agreements could be scoped into this guidance.

The proposed guidance may accelerate income or loss recognition on long-term contracts

Issue	Considerations
Long-term power sales agreements	For all power sales agreements not accounted for as leases or derivatives, the timing of revenue recognition may change. Accounting may be impacted by the Boards' proposal to supersede existing guidance for revenue recognition[1] as well as by the application of the proposed new guidance. This could potentially result in an acceleration of income or loss recognition depending on the nature of the contract.
Taxes collected from customers	Existing guidance that permits the recognition of taxes collected from customers and remitted to a government agency on a gross or net basis would be superseded. Such amounts would now be excluded from revenue (i.e. presented net).
Bad-debt expense	Credit risk would not be incorporated into the measurement of revenue. An allowance for the expected credit losses on receivables, as well as the impact of subsequent changes in credit risk, would be recognized in a separate line item classified within net revenues. This represents a change from the Boards' original proposal which would have required credit risk to be incorporated into the transaction price and subsequent changes to be recognized as a component of other income/expense.
Customer (contract) acquisition costs	An entity would recognize as an asset the incremental costs of obtaining a contract with a customer, provided the entity expects to recover those costs. The incremental costs of obtaining the contract are those costs that would not have been incurred had the contract not been obtained. This may impact the manner in which energy service companies capitalize customer acquisition costs.
Onerous performance obligations	In circumstances where the cost of satisfying a performance obligation will exceed the amount received (or allocated) as consideration to the performance obligation, the entire "loss" on the transaction would be recorded immediately. This guidance would only apply to performance obligations settled over a period of time greater than one year. This guidance may impact supply arrangements or power sales agreements that are not accounted for as derivatives but are "underwater" at the balance sheet date.
Alternative revenue programs	Although we expect that the existing ASC 980 guidance for alternative revenue programs will be retained, we understand that reporting entities would be required to separately disclose such amounts. The FASB has indicated that separate disclosure of such amounts will be a necessary requirement to retaining the existing recognition guidance.

[1] The FASB proposes to supersede EITF Issue No. 91-6, *Revenue Recognition of Long-Term Power Sales Contracts* and EITF Issue No. 96-17, *Revenue Recognition under Long-Term Power Sales Contracts That Contain both Fixed and Variable Pricing Terms.*

As constituent feedback is received and as we perform further analysis of the exposure draft, we will provide additional guidance on accounting issues and the potential impact on financial reporting.

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Questions

Clients of PricewaterhouseCoopers that have questions about this Power and Utilities Alert should contact their engagement partner. Engagement teams that have questions about this Alert should contact Casey Herman, Gavin Hamilton, Heather Horn, Andy Barclay or Bill Carlin.

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