Straight away

IFRS bulletin from PwC

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Key decisions propel the joint revenue project forward

What's new?

The FASB and IASB (the 'boards') met in April to discuss their joint project on revenue recognition. They reached tentative decisions on transaction price, variable consideration, contract fulfillment costs, licenses and customer put options. These decisions are tentative and subject to change.

The boards extended the target date for issuing a final standard from June 2011 to the end of 2011. The boards emphasised their focus on producing high-quality standards and evaluating stakeholder feedback.

What are the key decisions?

Determining the transaction price

The transaction price is the consideration that the entity is entitled to under the contract, including variable or uncertain consideration. It should be based on a probability-weighted estimate or most likely amount of cash flows expected from the transaction, whichever best predicts the amount to which the entity is entitled.

Allocating the transaction price

The transaction price is allocated to separate performance obligations based on the relative standalone selling price of the performance obligations in the contract. A residual value technique may be used to estimate the standalone selling price when there is significant variability or uncertainty in the standalone selling price of one or more performance obligations, regardless of whether that performance obligation is delivered at the beginning or end of the contract.

Pricing of individual performance obligations, including any discount inherent in the arrangement, should be considered when allocating the transaction price and when assessing subsequent changes. Some elements of the transaction price, such as uncertain consideration, discounts or change orders, might affect only one performance obligation rather than all performance obligations in the contract.

Recognizing revenue from variable or uncertain consideration

Revenue is only recognised when the transaction price is 'reasonably assured' of being received. Revenue is not reasonably assured when: (1) the customer can avoid paying additional consideration, such as when consideration is based on the customer's sales (for example, some sales-based royalties); (2) the entity has no experience with similar contracts or other persuasive evidence; or (3) the entity has experience, but that experience is not predictive.

Contract costs

Costs to fulfill a contract are in the scope of the revenue guidance only if they are not addressed by other standards. Costs required to be expensed by other standards cannot be capitalised under the revenue guidance. Costs likely to be in the scope of the revenue guidance include set-up costs for service providers and costs incurred in the design phase of construction projects. Fulfillment costs are capitalised if they are directly related to a contract (or anticipated contract), generate or enhance the entity's resources and are expected to be recovered. Asset recognition is required when the criteria are met.

Licenses

The distinction between exclusive and non-exclusive licenses in the exposure draft has been removed. Licenses should be evaluated under the same principles as other goods or services, with revenue recognised when the performance obligation is satisfied, which is when the customer obtains control of the rights.

Customer put options

Arrangements where a customer has the right to require the entity to repurchase an asset (a put option) should be accounted for as an operating lease under the leasing standard if the arrangement represents a right to use the asset over time rather than a sale.

Who's affected?

The proposal will affect most entities that apply US GAAP or IFRS. Entities that currently follow industry-specific guidance should expect the greatest impact.

What's the effective date?

We anticipate the final standard to have an effective date no earlier than 2014.

What's next?

The target date for issuing a final standard has been extended from June 2011 to the end of 2011. The key revenue issues yet to be re-deliberated include amortisation and impairment of capitalised costs, disclosure and transition.

Questions?

PwC clients who have questions about this *Straight away* should contact their engagement partner.