Via email:

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Dear Sirs

Discussion Paper: Preliminary Views on Revenue Recognition in Contracts with Customers

The Corporate Reporting Users' Forum (CRUF) welcomes the opportunity to comment on the Discussion Paper (DP) on Preliminary Views on Revenue Recognition in Contracts with Customers. As investment professionals, we place great importance on being able to compare and contrast the revenue figures reported by companies and so have followed the progress of this project with interest.

Our letter is a summary of the main areas of discussion amongst CRUF participants in Germany, the UK and the US.

CRUF participants are generally supportive of the direction of the DP. The majority of participants support the goal of a single, consistently applied, global standard on revenue recognition. However, they are concerned whether in practice a single set of principles-based guidance applied in politically, culturally and economically diverse settings would in and of itself result in more consistency and comparability. The Boards should address the risk that such a move could create a false impression of consistency and comparability, which would be a disservice to investors, through either disclosure or recognition, in order to help analyze the potential diversity in practice.

Most participants agree that it's appropriate to step back from the high volume of standards and related guidance that currently exist under US GAAP. Buy-side analysts, in particular, would appreciate a simpler, all-encompassing revenue recognition model that is consistently applied across different industries and regions. There is thus agreement with the Boards' approach in this area.

The use of a contract-based method was accepted by the majority of participants. There were, however, some reservations about whether or how investors would be able to assess the appropriateness of a company's revenue recognition policy given contractual terms are likely entity- and contract-specific and generally not disclosed. In addition, some participants wondered if this approach might be overly-legalistic, particularly for longer-term contracts that currently are accounted for using the percentage of completion method. There was some debate over how companies that use this method might react under a contract-based method. In particular, some participants thought that companies would change the terms of their contracts in order to ensure that title passed to the customer as work progressed, in order to be able to continue to recognize revenues in a similar manner to percentage of completion accounting. If this reflects the economics and value transfer inherent in the transaction, then such change to contract structures would be welcomed, if not then user analysis of economic activity might be distorted.

Some participants expressed their concern that the DP did not discuss what revenue is at a conceptual level instead immediately adopting a "balance sheet" centric approach to revenue recognition. This contract based approach means that revenues can only be realized on extinguishing a performance obligation. They believe that the Boards should at least have considered an "activity based" approach that would focus on measuring the performance of the business in terms of its activities during the period. Whilst we accepted the final position of the boards, users would expect to see sufficient disclosures that would permit them to analyze the company based on an "activity based" measurement approach if partially completed performance obligations are material. We believe that this is important information to understand value creation in the period if we assume that the business will remain a going concern and complete the contract. There is a dichotomy in accounting between a going concern principle and accounting for contracts, with the latter tending to focus on rights and obligations that would be enforceable even in the event of failure.

Participants, particularly those in the US, are concerned about how a single "principles-based" standard would be applied. It is clear that this would require preparers to use more judgment in determining when to recognize revenues, and how much to recognize in each period. There are two main concerns:

(1) Increased risk of abuse e.g. recognizing more revenues upfront than would be appropriate, and

(2) There will eventually be a reversion to "rules" in each industry and region. These may be developed and be interpreted in an ad hoc manner, and may not be as clearly articulated and consistently applied as under existing "rules-based" systems such as US GAAP as it currently exists.

Because of such concerns, participants on both sides of the Atlantic are not convinced that a single standard, in practice, would result in more comparability than presently exists without significantly enhanced disclosure. They see a risk that there could be a reversion to even less comparability.

There is unanimous agreement that disclosures would need to be significantly enhanced in order for a single "principles-based" standard to stand a chance of being successful. It is recommended that the Boards should consider disclosures in the next stage of the current project.

The most frequent example that was discussed concerning disclosures was the need to have more useful information to better understand the inter-relationships between the various accounts and activities that form the revenues cycle (especially changes in accounts where management applies significant judgment, such as sales related provisions), and between these accounts and actual cash receipts. There is a clear sense of frustration amongst participants that, in assessing past activities and in forecasting future periods, it is difficult to comb through the financial statements and piece together a useful interpretation of how the sum of these distinct parts add up to the whole. Some form of quantitative reconciliation between revenues, deferred revenues, customer billings, customer advances, unbilled revenues, accounts receivable, costs incurred and cash collected (or changes in major categories of deliverables under the DP approach, e.g. system, service, license, warranty, etc.) would be particularly helpful and should be disclosed in a tabular form for each reporting period at the operating segment level. Improvement to the quality of the accompanying narrative disclosures that would provide additional clarity on the matters outlined above should also be pursued.

Most participants are of the opinion that the Boards must consider cost recognition in this project. Revenues and costs are both sides of the same coin when it comes to measuring profitability, and focusing solely on one side might lead to unintended consequences and reduced comparability in reported earnings. It was noted that the removal of the detailed revenue recognition rules that currently exist under US GAAP might also result in a loss of guidance on how to account for the related costs in some instances. This would presumably necessitate replacement guidance and clear disclosures of these cases, absent a more rigorous consideration of cost recognition for the project as a whole. More broadly, it was generally agreed that there was concern over a potential lack of consistency in the amount and timing of cost recognition.

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About the Corporate Reporting Users' Forum (CRUF)

The CRUF came together in 2005 as a discussion forum to help its participants in their approach to the debate on current and future corporate reporting requirements. In particular, participants are keen to have a fuller input into the deliberations of accounting standard setters such as the IASB and FASB.

CRUF participants come from all around the world, including individuals from both buy- and sell-side institutions, and from both equity and fixed income markets.

The CRUF is a discussion forum. Different individuals take leadership in discussions on different topics and in the initial drafting of representations. It does not seek to achieve consensus views, though at times some or all of its participants will agree to make joint representations to standard setters or to the media. It would not be correct to assume that those individuals who do not participate in a given initiative disagree with that initiative.

We sign this letter in our individual capacity as participants of the Corporate Reporting Users' Forum (www.CRUF.com) and not as representatives of our respective organizations. The views expressed are those of individual CRUF participants and do not necessarily reflect the views of the respective organizations where we are employed.

The participants in the Forum that have specifically endorsed this response are listed below.

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