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Financial Accounting Standards
401 Merritt 7
Norwalk, Connecticut 06856
United States of America

30th March 2012

Re: Exposure Draft – Revenue from Contracts with Customers, revised

Dear IASB/FASB Board Members,

The Corporate Reporting Users' Forum (CRUF) welcomes the opportunity to comment on the revised Exposure Draft (ED) on Revenue from Contracts with Customers. We had reservations about the initial ED and we have been encouraged to note that many of our original concerns have been addressed. We think that the revised ED is a considerable improvement.

We also welcome the provision of illustrative examples, which helps us to understand the impact of the proposed changes.

The Japanese CRUF have provided a detailed analysis of their response to each question. For clarity, this is presented in full in appendix 1.

Underlying principles

We continue to support:

- The goal of developing a common revenue standard that can be applied consistently across industries, jurisdictions and capital markets.
- The core principle that revenue should be recognised when a company transfers goods or services to a customer and that the amount recognised should be based on expected consideration.
- The identification of separate performance obligations as the basis for recognising revenue for larger, more complex contracts.
- Improved disclosure. It is often impossible to extract useful information from the notes about when companies recognise revenue.

Question 1- transfer of control over time

We broadly welcome the inclusion of the option to recognise revenue continuously as long as certain criteria are met. However, we are not convinced that paragraph 35 is sufficiently clear and robust. In particular, we are concerned that the rules for continuous revenue recognition on long-term manufacturing contracts (e.g. aircraft) may well be too vague.

Question 2 – customer credit risk

We welcome the revised decision to present revenues before allowances for uncollectible debts. We do not have a strong view about whether bad debt expenses should be presented as a separate P&L item. We suggest that materiality should apply and that separate disclosure should only be required when losses from bad debts are material.

Question 3 – variable consideration

We welcome the use of a ‘most likely’ amount rather than probability weighting to estimate variable consideration when it is more predictive of the amount the entity is entitled to receive. In many cases, probability weighting results in a reported figure that does not match any of the potential outcomes, as well as introducing very subjective judgments when assessing probabilities. Some members are concerned that the revised ED might allow understatement of revenues as the paragraph seems to have been written only to prevent overstatement.

Question 4 – onerous performance obligations

We continue to feel strongly that onerous obligations should be assessed at the contract, not the performance obligation, level. Consider for example a company with a contract with multiple separate performance obligations. If some of the obligations are proving overly onerous but others are turning out better than expected, we would want all this to be netted off at the contract level. Forcing companies to recognise the onerous parts of the contract when the overall contract is on track will actually give a misleading view of reality.

We believe that the onerous contract test should only be applied to contracts lasting more than 12 months.

As we discuss later, we want to see tight limitations on the ability of companies to capitalise contract acquisition and fulfilment costs. In our view, ‘planned’ losses (such as the provision of products which, after an appropriate allocation of revenues, are still loss-making), that then lead to profitable service revenues, are in effect acquisition and fulfilment costs, not onerous performance obligations. While we prefer onerous performance obligations to be assessed at the contract level, we do not want to create a situation where companies can artificially smooth the profits on a long-term contract by deciding that the losses (or profits) in the early phase can be deferred.

Question 5 –disclosure in interim reports

The frequency and comprehensiveness of interim reports varies widely across the world and sometimes also inside individual countries. We think that companies should be encouraged to

make full disclosure of key metrics in interim reports but that the precise requirements should be left to local regulators, such as stock market regulators. Also, we think that interim reporting should, if necessary, be considered as a separate project in its own right, rather than introducing new requirements in a piecemeal fashion in individual standards that are intended to address other issues.

Question 6 – transfer of non-financial assets

No comment

Other issues

1. Capitalisation of costs. We are concerned that 1) costs to acquire and fulfil must be capitalised if recoverable and that 2) the guidance about what can be capitalised is too flexible. We think that companies should have the option to expense such costs and that their ability to capitalise such costs should be tightly constrained. This could all too easily become a gaping loophole for companies seeking to smooth earnings.
2. Disclosures. We generally welcome the additional disclosures. However, the additional disclosures should only be required if they are material. Also, movement in, for example, costs to obtain contracts should include separate headings for acquisitions/disposals and currency translation. Lastly, such disclosures are of limited use unless they are linked to the income statement and cash flow. It is very important for example to see how profits have been affected by the capitalisation of such costs. One of the CRUF's guiding principles is that it should be possible to reconcile the cash flow, balance sheet and income statement. We often feel that the boards pay insufficient attention to this important principle. We would not like to see the very limited reconciliation we have today reduced further.
3. Backlog and backlog analysis. We would like to see information about the outstanding performance obligations from contracts that have already started in accordance with the illustrative example provided. We would be happy for this to cover only contracts of more than 12 months' duration. We are however conscious that this could be an unwelcome and expensive extension of the scope of the auditor's work. We regard the provision of this information as desirable but not essential.

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.

Peter Reilly
Head of Capital Goods
European Equity Research
Deutsche Bank

Norbert Barth
Executive Director
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Terri Campbell, CFA

Peter Elwin

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General Manager
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Appendix 1:

CRUFJ's Comments on revised ED on Revenue Recognition

The Corporate Reporting Users Forum Japan (hereinafter the CRUFJ) welcomes the opportunity to comment on revised Exposure Draft (ED) on Revenue Recognition, Revenue from Contracts with Customers. The CRUFJ was organized in Tokyo in December 2009, and has been holding monthly meetings since then. Currently, there are 21 members including buy-side and sell-side equity analysts, credit analysts and portfolio managers. This comment letter reflects the discussions at the January and February meetings.

CRUFJ expects this comment letter to be read at various CRUF branches and incorporated into the final CRUF comment letter.

General Comments

The revised ED has been greatly improved to reflect actual practices compared to the original ED. Although the usability has been enhanced for both the user (investor) and preparer (entity), further refinements are necessary in some points.

Question 1: Transfer of Control of Goods or Services over Time

All members of CRUFJ think the revised criteria shown in Paragraph 35 are more understandable compared to the original ED. However, there are divided opinions among us regarding whether or not Para.35 provides necessary and sufficient criteria. We could not come to a single conclusion. The following are the opposing views among us regarding Para.35.

Supporting views:

— Paragraph 35 shows necessary and sufficient criteria for judging whether a performance obligation is satisfied over time. Para. 35(a) shows comprehensive criteria while Para. 35(b) shows supplemental criteria. It seems that 35(b)(i) shows the cases which might be frequently seen in the services industry, while 35(b)(ii) shows the cases in the transportation industry and 35(b)(iii) shows those in the construction industry. We understand Paras. 35(b)(i) through (iii) are not industry specific criteria and they can also be applied to other industries.

— Para. 35 provides satisfactory criteria. This paragraph will be clarified if it includes the explanations made in BC91 and other guidance.

Dissenting views:

— Para.35 is a mixture of principle-based criteria and industry-specific guidelines while it should be written simply on a principles-based approach. Thus it is too complicated. Para 35(a) describes necessary and sufficient criteria to be applied to the percentage-of-completion method. Criteria should be written simply in this matter. Para. 35(b), on the other hand, should be provided as indicators or guidelines. The attempt to describe Para. 35(b) as one of the criterion has complicated Para. 35.

Our suggestion is to define Para. 35(a) as the necessary and sufficient criteria for the principle-based approach. Para 35(b) should be indicators to merely supplement the criteria provided in Para. 35(a). If there are cases where Para. 35(b) does not suffice in determining when a good or service is transferred over time in accordance with Para. 35(a), more indicators or guidelines should be introduced or enhanced.

On another note, in order to say Para.35(a) represents necessary and sufficient criteria, we must reconfirm the following points:

- 1) “An asset” in Para 35(a) can be either goods or services, as set forth in Para 31.
- 2) The requirements on control to determine whether the “customer controls” an asset is defined in Para.37.
- 3) When Para 37 is insufficient to determine “control” for the continuous transfer of control method, more language should be added to Para. 37.

— Para.35 allows use of the continuous transfer of control method in a wide range of cases. We are afraid that Para. 35 will induce abuse of the continuous transfer of control method. For example, Para. 35(b)(ii) may cause abuse of the continuous transfer of control methods in the transportation industry. It is a problem if examples for the transportation industry are included in the criteria when the provisions still lack detailed criteria for the application of the continuous transfer of control method for transportation companies.

Question 2: Presentation of Profit or Loss from the Effects of a Customer’s Credit Risk

CRUFJ had disagreed with the original ED proposal of presenting net revenue after deducting customer’s credit risk on the income statement. Therefore we welcome the revised proposal of presenting gross revenue before deducting credit risk. However, we cannot come to a single conclusion whether the corresponding amounts in profit or loss

due to customer's credit risk should be presented as a separate line item adjacent to the revenue line item. The following are the opposing views among us.

Supporting views:

— Credit risk should stand out considering its importance. Amounts assessed as uncollectible (credit risk) by the entity is neither contra-revenue nor SGA expenses. Therefore we are in favor of the proposal that the corresponding amounts in profit or loss due to credit risk should be put below the revenue line. We agree that credit risk should not be hidden amongst SGA expenses but presented as a separate line item below the revenue line. This should enable analysts to use credit risk in their various analyses.

Dissenting views:

— Credit risk should be included in operating expenses, and not presented as a separate line item adjacent to the revenue line item. Credit risk is not material for most Japanese companies. Considering its materiality, it is not worthwhile to create a separate line to account for the effects of a customer's credit risk on the income statement.

The following are some additional opinions that were raised in regard to customer's credit risk.

— The definition of credit risk is unclear. This makes oblique the distinction between amounts that the entity assesses to be uncollectible which should be presented net of revenue and the effects of credit risk which should be presented gross of revenue. Credit risk is recognized in the following cases:

- (1) The client has gone bankrupt;
- (2) The client may not be bankrupt, however, the seller gives up collection of accounts receivable because collection costs surpass the collectable amount;
- (3) The client may not be bankrupt, however, the seller gives up collection for social or ethical reasons; or
- (4) The client may not be bankrupt, however, the seller gives up collection of accounts receivable due to fraud or dishonest acts on the part of the seller.

In the event that accounts receivables are only partially collected in the cases of (2) through (4) above, it may be difficult deciding whether the item should be reported as credit risk or contra-revenue.

Question 3 Constraint on the Amount of Revenue Recognition if the Amount of Consideration to which an Entity will be Entitled is Variable

- We agree with the proposal of setting constraints to revenue recognition if the amount of consideration to which an entity will be entitled is variable. However, we see the following issues in ED Para. 49
- ED 49 states that “the cumulative amount of revenue an entity recognises to date shall not exceed the amount to which the entity is reasonably assured to be entitled.” Application of this rule constraining the cumulative amount of revenue recognized is effective to prevent over-statement of recognized revenue but does not prevent under-statement. This provision should be rephrased to prevent the risk of under-statement of recognized revenue.
- Furthermore, the standards for whether an entity is “reasonably assured or entitled” to the amount allocated is ambivalent. It is unclear as to whether (i) variable consideration should be calculated only when the variable consideration is “reasonably assured or entitled” or if (ii) both fixed and variable costs are to be included in calculating the “reasonably assured or entitled” amount. The provisions should make clear the definition to ensure accurate calculation to enable the comparability of figures.

Question 4 Scope of the Onerous Test

- We agree with the proposed scope of the onerous test. We agree that the scope of the onerous test can be limited to contracts with a period of time greater than one year. Users do not seek onerous tests to be applied to short term contracts (such as a contract with only a month between the incurrence of performance obligation (contract inception) to the satisfaction thereof (recognition of revenue)). Requiring such information does not only place an unreasonable burden on the preparer of the financial statements but will also “cause material information to be buried in the flood of trivial information”.

Question 5 Revenue and Cost Disclosures for Interim Financial Reports

CRUFJ proposes that IASB should clarify the definition of “Interim Reports” in IAS Para.34. The term “Interim” varies among countries depending on whether half-year reports or quarterly-reports are prepared. For entities in Japan and the U.S., “Interim Reports” includes all three reports made through the financial year, for 1Q, 2Q, and 3Q. For entities that don’t prepare quarterly reports in Europe, however, an “Interim Report” corresponds to a half-year (2Q) report.

Requiring detailed disclosures for only the 2Q report or for all 1Q, 2Q, and 3Q reports will have significantly different implications. Japan has voluntarily introduced quarterly

reporting, but if detailed disclosures are required for interim disclosures, this would mean a large burden on the entities. Many entities believe that “2Q reports should provide detailed disclosures, but 1Q and 3Q disclosures should be concise.” Users are also of the same opinion that “2Q and 4Q reports should provide detailed disclosures, whereas speed is the primary objective of 1Q and 3Q reports thus detailed disclosures are not necessary.”

Question 6 Transfer of a Non-financial Asset that is not an Output of an Entity’s Ordinary Activities (e.g., Property, Plant and Equipment)

CRUFJ agrees with the proposal that an entity should apply the proposed control and measurement requirements to account for the transfer of non-financial. However we refrain from expressing our opinion on D17 Paragraph 69, sale of non-financial assets by entering into a financial lease. Lease accounting is now being revised and the renewal process is not yet finalized. At this point, we cannot judge if D17 Para.69 will fit the renewed lease accounting.